Introduction to Marketing

INTRODUCTION *to* MARKETING · PRINCIPLES OF WHOLESALE AND RETAIL DISTRIBUTION

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New York · 1948

PRENTICE-HALL · INC.

Printed in the United States of America.

Preface

THIS BOOK has a definite objective: to combine a treatment of general marketing methods and principles with a more detailed treatment of retailing, particularly the operation of small and medium-size stores. It is believed that one can not properly understand retailing without some knowledge of market economics and wholesaling. Students will understand retail store operation better if they first secure a general knowledge of the field of marketing and know the place of retailing in the overall picture. Therefore, market economics, the physical handling of goods, and wholesaling are treated before the discussion of retailing is begun.

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I

The Meaning and Scope of Marketing

DISTRIBUTION, or marketing is the most important part of business. Most business concerns can produce many more goods than they can sell at a profit. "Give us sales!" is the common cry of businessmen, and huge sums are spent on advertising and salesmanship. "Whatever can be sold can be made. The big problem is distribution." Such statements are common and may be accepted as generally true in normal times.

This condition has not always existed. Up until comparatively recent times, the big task of the race was to produce enough goods—food, clothing, and shelter—to satisfy its needs. During the past 150 years the problem has been altered by the use of labor-saving machinery; by the discoveries and inventions of chemistry, agriculture, physics, and engineering; and by the development of scientific management and accounting.

The development of the natural sciences and the arts of physics, entomology, geology, chemistry, management, and engineering has given us much new knowledge which has enabled us to increase greatly the output of goods and to reduce the costs of production. The result is that usually we are able to produce many more goods than the consumers are able to buy at the prevailing prices. Hence businessmen and farmers have become greatly interested in distribution. They wish to find buyers for their products and to increase the consumption of their goods.

Marketing a part of business. Business is divided into two parts—production and marketing. Production, in its business

meaning, has to do with the creation of goods. Distribution, or marketing, has to do with moving these goods from producers —factories, mines, and farms—into the hands of the consumers.

Marketing includes buying, selling, advertising, transportation, and warehousing. The corner grocer, the drug store, the chain store, the department store, the mail-order house, the wholesaler, the railroad, the grain elevator, the milkman, the livestock shipper, and the public warehouse are engaged in marketing.

Market distribution a part of economics. Economics has to do with the way we make a living and the way we live. For the purpose of this study, economics is divided into production, distribution, and consumption. Production, in the economic meaning, consists in the creation of utilities—things which satisfy human wants.

The chief utilities are form, place, time, and possession. Form utilities comprise goods and services. Bacon, washing machines, radios, airplanes, hats, dental service, and pictures are examples of form utilities. Place utilities are created when these goods are taken from the place of production to the place where they are to be consumed. Time utilities are created when these goods are kept until they are wanted. Possession utilities are created by getting goods into the hands of people wanting them. The creation of place, time, and possession utilities, in the economic meaning, is a part of production. If one is to have clothes, it is just as necessary that the cotton be stored until needed, brought to the places where the consumers live, and got into their possession, as it is that the cotton be grown and the cloth be woven.

Market distribution includes those activities which create place, time, and possession utilities. To the economist, market distribution is therefore part of production because it deals with the creation of utilities, and "distribution" refers to the *distribution of wealth* among the members of society. The businessman, however, thinks of distribution as selling his goods and getting them into the hands of the consumer. To the businessman, "distribution" means marketing—selling and transportation.

This difference of definition is confusing to the student. In order to use his terms correctly, it is necessary for him to remember whether he is talking to an economist or a businessman. In this volume, the businessman's definition will be followed. Production will be used to mean the creation of form utilities or the making of goods. Distribution will refer to the creation of place, time, and possession utilities or to the transportation and sale of goods and services—getting the goods from the farms and factories to the ultimate consumers.

Object of distribution. The object of market distribution, as well as of production (farming and manufacturing), is to supply human wants—food, clothing, and shelter. In addition to these primary wants, we have many other secondary ones. Our wants are expanding; the number of secondary wants seems almost unlimited. We have many more physical goods and personal services than our grandparents had, yet most of us desire many more than we have.

The larger the quantity of goods and services that people want, the greater the volume of business that is possible. As our wants are practically unlimited, business is capable of almost indefinite expansion. Distribution operates to satisfy the wants of people—to get the goods to them—and it often strives to increase the number of things which people want to buy.

Marketing needs study. Anyone expecting to make his living in the field of marketing needs a clear grasp of its principles. In marketing, as in many other fields of human endeavor, the problems may change but the principles remain the same, and one who possesses a knowledge of these fundamentals is aided immeasurably in solving his marketing problems.

Retail business failures occur daily; the failure of manufacturers and wholesalers is less common only because of their smaller number. Not all these failures are due to a lack of knowledge of the fundamentals of marketing, but a large portion of them could be avoided if marketing programs were planned more carefully. What is less apparent is that frequently losses or declines in profit are also due to inadequate understanding of the principles of marketing. Those who ex-

pect to engage in any phase of marketing should have a grasp of its principles if they are to be successful.

Those who desire to follow occupations in manufacturing, agriculture, banking, insurance, transportation, or one of the business professions such as accounting or production management need an understanding of marketing and its relation to their occupations. The major problem confronting a factory management in normal times is how to find and reach profitable markets. The farmer is frequently confronted with the same problem. Normally the question of manufacturers and farmers is not: Can we produce it? but: Can we market it profitably after we have produced it?

Bankers are concerned with marketing from the point of view of financing its operations, and insurance companies are interested in the risks connected with marketing operations. Transportation companies are interested in the movement of goods between markets. Accountants must understand clearly the operations of marketing in order to keep the proper records and make the proper reports. Production managers need an understanding of markets and marketing so that they may produce what the market will absorb.

The general managers of present-day corporations should have a clear view of their organization's various operations because of the necessity of keeping them all in balance. Consequently, they need an understanding of marketing principles and functions in order to keep the various departments operating smoothly. Lack of co-ordination between the marketing divisions and the other divisions of a business results in inefficiency and higher costs.

Methods of studying marketing. Market distribution deals with services, goods, and men. In order to market goods, services must be rendered, acts performed, things done. These services or acts are commonly called *functions.*

One method of studying marketing is to take up a study of the functions involved. This is called the *functional* appro[redacted]ch, or method.

Another way to study marketing is to[redacted]tuav [redacted]rious goods, or commodities, that are markete[redacted] t[redacted]b[redacted]the

ways in which they reach the consumers. This is known as the *commodity* approach, or method.

The third method of studying marketing is to study the operations of men engaged in marketing. These are called middlemen or institutions. This method is known as the *middleman,* or the *institutional,* approach.

In using the functional approach, we see what services or functions are performed; what goods they are performed upon; and what middlemen perform them. In using the commodity approach, we see what goods are marketed; what functions are performed upon them in the distributing process; and what middlemen perform these functions. In using the institutional approach, we see what institutions, or middlemen, are engaged in distribution; what functions they perform; and what goods they handle.

Advantages of functional approach. The study of marketing functions draws our attention to the operations or services performed in distribution. A study of these services helps us to analyze the distribution process, to see just what is done, how it is done, why it is done, and who does it.

The same function may be performed once or several times; sometimes a study will point out ways of reducing the number of times a thing is done. For example, a certain product may be graded every time it is sold. The adoption of uniform standards and the grading by government-licensed inspectors may mean that one grading is sufficient for the entire marketing process. All buyers and sellers may buy and sell on the grade established by the government inspectors.

It is often said that there are too many middlemen. If a middleman is eliminated, are his functions eliminated or are they transferred to others? A study of functions should help us to answer such questions.

Advantages of commodity approach. The commodity approach starts with familiar goods. It is a simple and easily followed method. The disadvantages of this method are that it requires long descriptions of goods and operations and involves much repetition, if all commodities are studied. The commod-

ity approach seems best adapted to the study of farm products and industrial goods (Chapters 7-10).

Advantages of middleman approach. The institutional approach considers the operations of various middlemen. It is a very practical approach, especially for the student who later enters business. The danger of the institutional approach is that it may become too descriptive. It is not as analytical as the functional approach.

We shall devote considerable attention to the operations of middlemen, but before doing so, an explanation of the various marketing functions will be given.

The Basic Marketing Functions

Marketing functions can be divided into those that deal with change of ownership, the general business functions, and those that deal with the physical handling of goods. The latter are discussed in the following chapter.

Buying function analyzed. The acts which a buyer performs may be classified as follows:

1. Determining needs;
2. Finding sources of supply—sellers;
3. Negotiating prices and other terms;
4. Obtaining title to the goods (legal part of buying).

1. *Determining needs.* Buying begins when the prospective buyer become conscious of a desire. This desire may be aroused by chemical changes in the body as in the case of hunger, or the desire may be aroused by any of a variety of things in the individual's environment. The sight of a neighbor's new car may so arouse the desire of the onlooker that the latter purchases a new car also. The desire of the prospective industrial buyer is aroused as a result of the competitive struggle. He wishes to make economies which will result in lower prices and increased sales, or his desire may be to reduce the costs of operation and thus increase profits.

After the desire has been aroused, the [illegible]ecti[illegible]aser is confronted with determining the [illegible] will

satisfy the desire. The process may be fairly simple in the case of selecting a particular food to satisfy hunger. In selecting furniture or an automobile the process is likely to take longer and involve the exercise of considerable judgment. The determination of the specific product needed to satisfy a desire of industrial purchasers may involve the careful study of some problem of the plant or store.

2. *Finding sources of supply.* The location of a source of supply for a given product may involve no more difficulty for the consumer than going into a retail store where the article in question is customarily sold. For the professional buyer who represents large industrial consumers, the location of sources of supply may be one of the most difficult functions that he performs. At times, however, it involves little more than looking into the appropriate directory of manufacturers or other producers.

3. *Negotiating terms.* The opening of negotiation of terms may be made in a variety of ways ranging from the mere nod of the head at an auction sale to the sending of a cablegram halfway around the world. Other methods may range from a simple want ad in the daily newspaper to the submission of elaborate written proposals and specifications.

At times the household consumer gives very little attention to the matter of price before he makes a purchase. In the case of larger purchases, such as an automobile or home, the matter of price is given more attention. The industrial consumer is likely to be represented by a professional buyer who will use considerable skill in ascertaining and negotiating prices and other terms.

In wholesale buying, finding out the prospective seller's willingness to sell is sometimes important in determining what kind of an offer to make and what price to offer. The offering of a price may be by a sign as at an auction or on the floor of a commodity exchange. Payment to the seller is made in a variety of ways and it may be made immediately or it may be postponed through the medium of a charge account or a conditional sales contract.

4. *Obtaining title.* Legal title to goods must be obtained

before a purchase is completed. The title may be transferred by a formal document but in the majority of purchases acquiring legal title is not formal. Title may be understood to pass when the goods are received by the buyer.

Selling function analyzed. Selling, like buying, is composed of several actions. The actions which the seller performs may be classified as follows:

1. Creating demand;
2. Finding buyers;
3. Giving buyers advice;
4. Negotiating terms;
5. Transferring of title.

1. *Creating demand.* By creating demand we mean arousing the desire for goods among people who have ability to buy them. If people can be made to want things badly enough, they may work harder or more intelligently in order to secure the money with which to buy them. Some explain the development of civilization by saying that people were made to want things, and, in order to satisfy their desires, they worked and schemed. As a result of their efforts came development. According to this reasoning, the salesman and the advertiser who arouse our desires for new or better things help to develop civilization. On the other hand, some say that we are over-sold and are too burdened with things to get the most enjoyment out of life.

New things, better things, more beautiful things are constantly being placed on the market. The seller may use advertising, personal salesmanship, or publicity to create demand. He may display and demonstrate the goods, give away samples, and try to "educate" the buyers to the advantages of his product. Much advertising and a goodly portion of personal salesmanship are used to create demand.

2. *Finding buyers.* A good deal of the selling effort is made to find people who already want the product; want ads, for example, are almost entirely directed to people who are already conscious of a need. Many retail salespeople assume that people know what they want when they enter a store. Some travel-

ing salesmen are in reality "order takers"; they simply fill the requests of people who already desire the goods offered by the salesmen. The bulk of price advertising is aimed at people who already want the goods.

3. *Giving advice.* The seller often gives advice to buyers. This advice may relate to the product's use, or it may be much broader and be given to help the buyer determine his needs or to conduct his business more efficiently. Many buyers depend upon the sellers to teach them to use and repair their goods. By helping the buyer to secure the best use from his products, the seller creates satisfied customers and a reputation for his goods—both results help to increase sales. The seller may go farther and help the buyer with the conduct of his business; he may give advice on stockkeeping, advertising, window display, bookkeeping, buying, or salesmanship. He does this to build up goodwill and to make the buyer a better businessman so that the latter will sell more of the seller's goods.

4. *Negotiating terms.* Many retail stores have adopted the one-price policy; the customer either buys at the specified price or does not buy at all. He may, however, shop from store to store for a lower price. In wholesale markets the buyer frequently strives eagerly to obtain the best possible terms from the seller. Many sellers may be after the same order. Credit terms, time for delivery, payment of transportation costs, repair service, guarantee, and other terms may be negotiated.

The functions involved in the physical handling of goods are discussed in the following chapter.

General Business Functions Involved in Marketing

Certain functions are performed by business organizations generally and not by marketing organizations alone. Among these functions are financing, the bearing of risk, and recording.

Financing. In the operation of a business, funds are needed to buy merchandise, to extend credit to customers, and to pay operating expenses. The sources of the funds and the methods of obtaining them vary but the principles of sound financing should be followed.

The major portion of the long-term investment or capital for a marketing organization should be provided by the owners. Funds which are needed to finance temporary expansions in the inventory or the accounts receivable may be obtained from banks or from merchandise creditors. Wholesale and retail organizations should not, as a rule, obtain capital by the sale of bonds and preferred stock. A bondholder is a creditor and has the right of foreclosure if interest or principal is not paid on the due date.

Not only must marketing organizations themselves be financed but they find it desirable to extend credit to their customers by the installment method or on open account and thus perform the financing function. The installment method is usually more expensive than the open account method. The installment method requires periodic payments until the original amount of the debt plus interest is paid. The open-book account is usually paid in a lump sum in a short time.

Risking. When any action is taken without knowledge of what the results will be, or with the possibility that the results will be adverse as well as favorable, risk is borne. Thus, risk-bearing is inescapable. The businessman who has great knowledge of his industry or business bears less risk than one who possesses inadequate information. The businessman with the most knowledge of his industry is in a better position to judge the possibility of adverse results than one who has little knowledge or experience. Frequently risk is borne without the knowledge that it is borne. Even if the risk is recognized, the amount of the risk which is being borne may be estimated incorrectly.

Many risks arise from the ownership and use of property although business risks may be classified in other ways. Whoever acquires title to goods bears risks which non-owners of goods do not bear. Risks may be classified as follows:

A. Ownership risks:
   1. Decline in price of goods;
   2. Change of fashion causing goods to be sold at a loss;
   3. Damage of goods by fire, smoke, or water;

4. Loss of goods by theft, robbery, burglary, or embezzlement;
5. Damage of goods by flood, tornado, lightning, moisture, hail, heat, or drought;
6. Decay or loss due to vermin;
7. Change in demand for goods because of technological improvements or depression;
8. Damage by rioters or civil commotion.

B. Financial risks:
1. Accounts and notes may become uncollectible;
2. Theft, robbery, burglary, or embezzlement of money and securities;
3. Loss of money through failure of financial institutions;
4. Decline in price of securities owned.

C. Liabilities for injury:
1. Trucks or salesmen's cars may injure persons or damage property;
2. Customers may be injured on premises;
3. Goods may be defective and injure the customer;
4. Employees may be injured while at work.

D. Liability on contracts:
1. Advances in wages or the price of materials may cause the cost of fulfilling future contracts to increase;
2. Default of others may cause loss on joint contracts;
3. The guarantee of goods may involve loss on replacement or repairs.

E. Liability of loss of key men:
1. Important managers or skilled workers who have had expensive training may die, become ill, be injured, or resign.

F. Weather risks:
1. Sales may be lost because of bad weather.

Shifting risk. The businessman does not have to carry all these risks himself. Many of the risks just enumerated may be shifted to insurance companies. Loss and damage because of fire, tornado, theft, automobile accidents, and injuries to em-

ployees are often insured against. Insurance also may be carried against other hazards such as embezzlement, rain, hail, and losses from bad debts. Certain other risks, such as changes in fashion and some declines in prices, cannot be insured.

When risks can be shifted to insurance companies, the cost of the premiums can be included in operating expenses. Owners are then willing to operate for slightly smaller profits. Insurance companies frequently base their rates on average losses, and such rates are usually less than the anticipated earnings necessary to induce individuals to assume all risks. A merchant may be ruined if his store burns and he has no insurance. The risk is so great that he feels he cannot carry it himself, therefore he shifts the risk to an insurance company. He feels safer and does not need as large a profit to induce him to stay in business. The cost of marketing is thus reduced.

The insurance company must charge more than enough to cover the risks accepted. It has expenses for selling, overhead, and adjustments which may equal from 25 to 100 per cent of the losses paid. Policyholders must therefore pay more for insurance than the cost of the risk involved. For this reason most businessmen prefer to bear some risks themselves, particularly risks which they feel are less likely to cause losses. They must also carry the risks that cannot be insured.

Guarding against risks. The businessman can do much to reduce the amount of risk. Fire damage is lessened by fireproof buildings and automatic sprinklers. Risk of theft and burglary is reduced by good locks and vigilant watchmen. Losses from bad debts may be reduced by a careful check on applicants for credit and by an aggressive collection department. Risk of changes in fashion may be limited by careful fashion forecasting and the purchase of fashion goods in small quantities. Loss from price declines may be lessened by detailed market forecasting and a rapid turnover of stock. Injuries to employees may be reduced by safety devices and adequate job-training of workers.

Risks increase marketing costs. Risks account for a part of the cost of marketing. The importance of risk may be seen easily when the dealer handles fashion merchandise or perish-

able goods. Such goods may drop in value or become unsalable as a result of rapid changes in style or early decay.

Recording. Accounting, or recording, is necessary in many transactions. Sales slips, order blanks, stock records, invoices, bills of lading, and checks are usually recorded. Ledgers are posted and expenses and income are itemized, classified and analyzed.

The businessman is often at a loss to know just how full and complete his records should be. Accounting involves expense, but it provides facts upon which the businessman can base his operations. The present opinion is that most business concerns have devoted too little attention to efficient accounting procedures. Records can be used to reduce expenses and to increase profits. Although full records are often needed, time should not be spent in keeping records that are not used.

Marketing Organization

Organizations engaged in marketing. When marketing functions must be performed on a large scale, at great distances, and at uncertain times, organizations are necessary to perform them. The organizations as well as individuals may designate various agents to act for them in the performance of these functions. These organizations and individuals are (1) those engaged in the extractive industries such as farming, fishing, and mining; (2) manufacturers of both goods and services; (3) merchants, who may be divided into wholesalers and retailers; and (4) consumers, who may be divided into industrial and household consumers.

Mining companies, lumbering companies, farmers and others are engaged in obtaining natural resources from the earth with the object of selling them to manufacturers who will convert the raw materials (ore, lumber, wheat) and resell them. Some of the products, if in proper condition, may go direct to the household consumer from the organization or individual who extracted them from the earth. Public utilities and insurance companies, for example, are engaged in producing services which go directly to household or industrial consumers.

Wholesalers and retailers obtain commodities from the extractive industries (farming, mining, sawmilling, and fishing), or from manufacturers. Manufacturers, the extractive and service industries, and individuals, wholesalers and retailers also consume products and services in their operations and as such are industrial consumers. The chief problem for both industrial and household consumer is to get as many commodities and services as possible for each dollar spent.

Those who buy in order to resell are mutually dependent upon each other. If the commodities which they buy are not resold easily and quickly, both buyer and seller suffer losses or reductions in profit. Consequently, it is customary for manufacturers, wholesalers, and retailers to render each other mutual aid in their advertising and selling efforts.

Executive division of labor in marketing. In order to perform the marketing functions efficiently, the various groups assign the management of different phases of marketing to individuals who are skilled in the performance and management of those phases. The manner in which the marketing work is divided varies according to the kind of activity performed. In many organizations, however, will be found a sales manager, an advertising manager, a purchasing agent, and a credit manager. Some organizations also have a traffic manager.

The sales manager. It is the responsibility of the sales manager to obtain a profitable volume of sales. This does not always mean a large volume. A small volume of merchandise with a large profit margin may yield a greater net income than a large volume of merchandise which is easy to sell but is sold on a small margin. The sales manager's work involves the selection and training of salesmen, the establishment of compensation methods, the assignment of territories, the setting of quotas, the studying of salesmen's expense and sales reports, the conducting of contests, and the planning of campaigns, conferences, or conventions. His duties may also include the supervision of the advertising department.

In carrying out his work, the sales manager should know the location of the chief markets for his company's products. He should be familiar with the provisions and common interpreta-

tions of the laws which regulate prices and methods of competition. He should know what advertising and selling practices constitute unfair competition. He should know the strong and weak points of the various methods of distribution. He should have a thorough knowledge of the various factors which affect the demand for his products. He should understand the basic human desires and the appeals which his merchandise can utilize in fulfilling these desires. He should also understand the interrelationships of other departments with his own.

The advertising manager. It is the responsibility of the advertising manager to stimulate desire for his company's product or service. His work may include the selection and analysis of media, preparation of campaigns and reviewing the results, conducting market research projects, purchase of illustrations, selection of advertising personnel, preparation of the advertising budget, supervising the preparation of copy, illustrations, packages, dealer helps, mailing lists, and co-operation with advertising agencies.

Like the sales manager, the advertising manager should understand the basic motives and desires of human beings and what appeals the products of his company can make best. He should know the laws of attention and be able to express ideas clearly and attractively. The processes involved in manufacturing the product and the various uses to which the finished product is put should also be a part of his knowledge. He should be familiar with the laws which regulate advertising practices.

The purchasing agent. The purchasing agent for an industrial company or an institution is responsible for obtaining necessary raw materials, supplies, and equipment as economically as possible. This does not mean that he is constantly searching for the lowest price because he knows that low price and economy are not one and the same thing. The work of the purchasing agent involves searching for sources of supply, receiving salesmen, studying price trends, supervision of inventories, testing products, placing claims, and the preparation of the purchasing budget.

The purchasing agent should understand the various factors affecting the prices of the items that he buys. He must understand what contributes to the quality of those materials, supplies and equipment. He should know the provisions of the laws which regulate prices and the decisions relating to fair competition which affect purchasing. He should have a thorough knowledge of the technique of salesmanship.

The credit manager. It is the responsibility of the credit manager to extend credit in such a manner that sales volume is increased and large losses are not suffered as a result of bad debts. The credit manager gathers and analyzes information about customers, reports inactive accounts to the sales department, furnishes salesmen with information about prospective customers, co-operates with local and national credit organizations, writes collection letters, looks after the interests of his company in cases of bankruptcy, and handles repossessions of merchandise.

In carrying on his work, the credit manager must know the current position of the business cycle since the trend of business has a direct effect on credit policy. The credit manager should know what the rights of his company are in cases of bankrupt creditors and in disputes over sales. To aid him in his analysis of financial statements he should know the performance standards and credit ratings of the various industries to which his company may sell.

The traffic manager. The traffic manager is responsible for obtaining economical and efficient transportation for his company. His work includes study and selection of routes, study of freight rates, handling of claims against carriers, direction of cases before regulatory commissions, arranging for an adequate supply of cars (railroad, trucks, etc.), auditing bills, and the study of economical and safe packing methods.

To perform his various tasks efficiently the traffic manager needs a knowledge of freight rates. He should also know the chief routes of the various kinds of carriers, the principles underlying freight classification, the laws regulating transportation, the method of procedure before regulatory commissions, and the shipping and packing requirements of the carriers.

Questions

1. Define marketing or distribution.
2. What is the relation of distribution to business?
3. What is meant by *utility?* What utilities are created in the process of distribution?
4. What are the two meanings of distribution?
5. What is the object of marketing?
6. What are the three ways of studying market distribution? What is the chief advantage and disadvantage of each method?
7. What are the two basic marketing functions? Can a market be said to have existed if these two functions are not performed at some time?
8. What are the subdivisions of the buying function? Is the "buying function" a class of functions? Must some of the subdivisions or subfunctions always be performed before a purchase can be completed? If so, which ones?
9. What are the subdivisions of the selling function? Is the "selling function" a class of functions? Must some of the subdivisions or subfunctions always be performed before a sale can be completed? If so, which ones?
10. What utilities are created by the performance of the functions of buying and selling? Explain.
11. It is said that we have too much salesmanship—that we are "over-sold." It is said that we need more *buymanship,* meaning that the consumers should devote more time and attention to buying. Comment on these statements.
12. It has been said that the desire for things is the main factor in causing people to work, and that only as a result of work has civilization been developed. According to this viewpoint, the person who makes people want more things is a benefactor of mankind. Do you believe that people are benefited by being made to want more things?
13. It was formerly the practice for retail dealers to mark their prices in code and for the sellers and buyers to higgle over prices. Higgling is still common in many foreign countries. By the "one-price policy" we mean that the seller places his price on the goods; that the same price applies to all comers; and that he will not sell for less than the marked price. What are the advantages and disadvantages of this policy?
14. Why is there more higgling over prices in the wholesale than in the retail trade?
15. What general business functions are involved in marketing? Are they really a part of buying or of selling?
16. Define or explain the following: financing, risking, recording.

17. What are the principal kinds of risk?
18. Which risks can be shifted? How?
19. What are the "organizations" engaged in marketing? Are the fundamental marketing problems of these "organizations" different? If so, how?
20. Who are the principal marketing executives? What should be the training of each of these executives? What are the responsibilities of each? In general, which executive is likely to be the most highly paid?

2

The Physical Handling of Goods

In the physical handling of goods the marketing functions of transporting, packing, assembling, dividing, storing, standardizing, and grading are performed. Standardizing does not necessarily involve the physical handling of the goods, but it does involve the consideration of the physical characteristics of the goods.

Transportation

Transportation moves goods from the places where they are produced to the places where they are consumed, thus creating place utility. Transportation also creates time utility because goods are moved when they are wanted.

When transportation methods work smoothly and efficiently we are not aware of the fact that they create time utility, but let some transportation method fail to deliver goods to us when we want them or expect them and we are keenly aware of a loss in value. Shippers of farm products can suffer loss if their products are not delivered promptly to the wholesale markets. If there is a delay of a few days or perhaps hours, the market price may decline and the shipper will receive a lower price than he would have received had his products reached the market sooner.

Transportation is a powerful factor in the development of markets because it connects sources of supply with demand. In the days when we lacked adequate transportation facilities our

markets were small and local. Nearly everything which was consumed in a town or village was produced there or near-by. National markets did not exist until after the development of the railroad system and the establishment of transcontinental lines.

The connection of manufacturers and farmers in all parts of the country with consuming markets facilitated the development of regional divisions of labor. Each region or territory could specialize in what it could produce most profitably and in so doing they became larger markets for other regions. A given region was able to buy more of the products of other regions.

The development of efficient communication systems has also had a profound effect on the growth of markets. With improved methods of communication, information concerning demand and supply conditions is spread widely and quickly. For example, fashions changing rapidly or prices reflecting minor factors of supply and demand, may cause goods to be directed to other markets or not shipped at all. The right quantity and the right quality of goods are more likely to be shipped to the right place at the right time.

Goods are moved by railroads, trucks, barges, ships, airplanes, pipelines, animals, and human beings. Local transportation appears to cost more than rail transportation. The handling of goods between factories, stores, warehouses, trucks, and freight cars is one of the most expensive phases of transportation. One study showed that the cost of packing, carting, loading, unloading, and unpacking twenty commodities was nine times as much as the freight paid to the railroads for moving the shipment.

The motor truck is used in local transportation. It is a feeder for the railroads and is also an important competitor of the railroads for long-distance traffic. The airplane offers great possibilities and is already important in carrying passengers, express, and mail. Pipe lines are important in moving oil and gas. In international trade, water transportation is necessary. In the United States, inland water transportation is relatively unimportant except for the movement of iron ore, coal, limestone, grain, and other commodities on the Great Lakes.

The passenger automobile, the streetcar, the motor bus, and the railroad are the important agencies for passenger transportation. In total mileage the automobile comes first.

Services rendered by railroads. The railroad moves freight in carload lots (c. l.) and in less-than-carload lots (l. c. l.). Rates on the former are lower. Carload freight is handled in larger quantities, and the shippers usually load the goods into cars at the place of shipment and unload the goods from the cars at their destination. The railroads place ("spot") the cars on sidings convenient to the shippers. Less-than-carload shipments are usually loaded and unloaded by the railroad employees. In the past, the rail haul began and ended in the rail terminals. If a shipper did not have a siding, he delivered his goods to a railroad-owned siding or freight house. The Railway Express company for many years has picked up packages from the shippers' doors and delivered them to the door of the consignees. This pick-up and delivery service, known as "store-door delivery," is performed by motor-truck carriers. In order to meet truck competition, many railroads are giving free store-door delivery on less-than-carload shipments. The practice can also be applied to carload shipments.

A common carrier is one who holds himself out to the public to move goods or persons for pay. A common carrier should not be confused with a carrier for hire, who moves goods or persons under special contract and does not hold himself out to move goods for anyone who may apply. The common carrier must serve all equally at reasonable prices. He cannot refuse service as long as he has facilities available. He is responsible for the safe delivery of the goods or persons in his care. He is excused for damage to goods or injuries to persons only for such causes as acts of God, acts of a public enemy, acts of shippers, acts of public authorities, or loss caused by the inherent nature of the goods. This heavy responsibility upon the common carrier seems reasonable, since the shipper ordinarily cannot tell when, where, or why his goods are lost or damaged while they are in the hands of the carriers.

The contract between the railroad and the shipper is called a bill of lading. The bill of lading is a receipt for the goods,

a contract for the transportation of the goods, and a shipping order.

There are two kinds of bills of lading. The straight bill is used for ordinary shipments. A copy is sent to the consignee who must present it to obtain the goods from the carrier. The order bill is used by the shipper when he wishes to collect from the buyer (consignee) before the buyer obtains the goods. The seller ships the goods ordered, prepares a bank draft on the buyer, attaches the draft to the order bill, and sends both to the buyer's bank for collection. When the buyer pays the draft, the bank delivers the bill of lading to him. He takes this to the railroad and obtains the goods. The order bill of lading carries title to the goods and is negotiable.

Shippers and receivers are allowed a stated amount of free time in which to load and unload cars. The interval is usually 48 hours, commencing at 7 A.M. on the day following (1) the spotting (placing) of cars, or (2) issuance of the notice of arrival. If cars are held longer, an extra charge known as demurrage is made.

Many goods are shipped before they are sold and are sold while they are in transit. The shipper then changes the destination of the goods, a procedure known as diversion. When goods reach their destination, they may be reconsigned to another point. The through rate from the point of origin to the new destination applies when shipment continues in the same direction, but an extra charge for the reconsigning privilege is added. This is usually considerably less than the sum of the local rates which are charged when the diversion and reconsignment privilege is not allowed.

While in transit, goods are often stopped for manufacturing, storing, feeding, grading, pressing, or fabricating. Shippers are often allowed in-transit privileges; they pay only the through rate from the point of original shipment to the destination of the processed goods plus a relatively small in-transit charge.

Services performed by motor trucks. Motor trucks are a very important part of our transportation facilities. They are engaged very largely in local service: delivering retailers' and wholesalers' goods to the customers, hauling goods to and from

the railroad terminals, hauling goods from farms to shipping stations, and moving goods within cities.

Trucks, however, are moving more and more goods between towns served by the railroads. Even if the cost of moving goods by truck is higher than the railroad rates, the truck may be used because of other economies. It moves goods from store door to store door. When less-than-carload shipments are made by rail, the goods must ordinarily be loaded on the truck, hauled to the freight house, unloaded, loaded into a freight car, unloaded at destination, loaded into a truck, hauled to the store of the buyer, and unloaded. If a motor truck is used, it may load the goods at the shipper's door and carry them directly to the warehouse of the receiver. Thus one motor haul is substituted for two motor hauls plus one rail haul.

For long distances the railroad appears to have lower costs, owing to the fact that a train moves a much larger load than does a truck. A freight train with a crew of five men may move from 2,000 to 10,000 tons of freight, or 400 to 1,000 tons per man. A man on a motor truck may move anywhere from a few hundred pounds up to 5 or 10 tons. If the average load per man on a freight train is 600 tons and the average load per man on a truck is 3 tons, then one man on a freight train moves 200 times as much as one man on a truck. Despite this ratio the movement of goods by truck has grown tremendously.

Goods are moved by truck for hundreds of miles and hauls of over 1,000 miles are not unusual. Some of the increase in truck transportation is due to the quicker deliveries and the flexible routes of trucks; to the convenience of store-door deliveries; to the avoidance of delays and damages in rail terminals; to savings in crating and handling costs; and to the shortening of trade channels and the lessening of other marketing costs. Truckers often buy goods at the place of production and sell to buyers at the destination, a procedure that frequently saves the expense of handling by one or more middlemen. Trucking often reduces marketing expenses so that total marketing costs can be reduced even though higher transportation costs are incurred. In periods of business depression, many trucks are operated by owners who would otherwise be unemployed. They buy or

rent trucks (often used trucks) and go into business for themselves. They may be willing to work very cheaply until business improves sufficiently for them to get better jobs.

It is doubtful whether the tax systems of many states require the truck operators to pay their proportionate share of the costs of building and maintaining the highways. If this share is not paid, the trucks are given an artificial advantage over the railroads which must build, maintain, and pay taxes on their roads.

Services of passenger automobiles. The automobile has probably done more to influence our methods of living and consequently our demands for goods and services than any other invention since the steam locomotive. The automobile furnishes fast transportation adapted to the needs of the individual. It has led to the building of a wonderful system of paved highways. It has increased travel, brought formerly isolated communities into touch with the outside world, helped education, and shifted retail trading areas. Furthermore, it has increased the mobility of trade. The family with a car does not have to trade at the nearest store but can visit those located at a distance. The automobile has changed our methods of living and so affected our demand for goods and services.

The automobile and truck have also affected business methods. Many traveling salesmen use automobiles to reach a much wider territory. The motor truck has increased the frequency and speed with which goods are delivered from producers to jobbers and retailers.

Storage

Storage, the keeping of things from the time they are produced until they are needed by consumers, creates time utility. It provides the consumer with an even or regular supply of goods throughout the year, although many goods are produced only at certain seasons. Wheat, corn, cotton, tobacco, and apples are harvested during relatively brief periods, but the public wants these products every day. Storage is necessary to supply this continuous demand.

The production of many other goods is irregular. Cows nor-

mally give more milk and hens normally lay more eggs in the spring and summer than during the fall and winter, but consumers want about the same quantity of milk and eggs throughout the year. Storage is therefore utilized to retain some irregularly produced products from the period of surplus production to the period of deficient production. Without storage, prices would be so high during the fall and winter that many of us would have to go without butter and eggs. On the other hand, spring and summer prices would be so low, owing to surplus production, that the markets would be demoralized and the farmers discouraged.

Storage facilities and services. Storage facilities may be provided by producers, middlemen, consumers, or warehousemen who store goods for pay. Goods are stored in farmers' granaries, manufacturers' storerooms, retailers' stores, consumers' pantries, and public warehouses. It is very important that adequate storage facilities be available at all times: sufficient space in properly located buildings, proper protection against fire and theft, and proper temperatures.

Some goods are nonperishable and require no special protection. Ores, pig iron, and rough lumber are often stored in the open, while relatively nonperishable goods, such as grain, cotton, wool, and dressed lumber, need only be kept in dry places. Some products are semiperishable; they can be stored for considerable periods under proper conditions. In this class are such products as apples, butter, and potatoes, which should be kept cool and at even temperatures. They are often stored in cold-storage warehouses. Some goods are highly perishable, peaches, strawberries, tomatoes, and fluid milk, for example, and can be stored only for short periods.

New and improved methods of storing have increased the number of products that can be stored successfully. Quick freezing at very low temperatures has changed the marketing of many products. It has enabled fresh ocean fish to be marketed all over the country. The method is also being used on fresh fruits, vegetables, and meats to permit lengthy storage periods for these products.

Storage tends to equalize prices. Let us take butter as an example. The heaviest production comes in the spring, and since the price drops at this time, dealers buy butter for storage. Their demand keeps the price from dropping as low as it otherwise would. In the fall and winter, when less butter is produced, the storage product is placed on the market, and the additional supply keeps the price from going as high as it otherwise would.

The demand for many products is seasonal or irregular. Electric fans are purchased chiefly during summer heat waves. Ice skates and sleds are sold in largest numbers during the winter. The biggest volume of jewelry and toys is sold just prior to Christmas. Fireworks are sold principally for the Fourth of July. Bathing suits, fishing tackle, electric heaters, gloves, and hunting supplies are also seasonal in their sales volume. If factories producing such seasonal goods are to be operated regularly, part of the goods produced during the dull months must be stored to meet a later demand.

Reserve stocks are necessary to guard against interruptions in production and transportation. Production may be interrupted by fire, strikes, floods, droughts, and other causes. Some manufacturers keep large reserve stocks in company depots outside their factories to care for their customers in case production is stopped.

Transportation may be interrupted by storms, strikes, wrecks, or floods. Ice stops water transportation on northern waters during the winter. Motor-truck transportation is often interrupted by snow and ice. Supplies are often stored near the consumers to provide goods and service despite the interruptions in transportation.

Cost of storage. Storage involves cost for space, for labor in placing goods in the storage warehouse and taking them out, for interest on the capital tied up while the goods are in storage, for insurance, and for loss and deterioration of the goods. Storage also involves risk. Goods may shrink in weight, rot, be stolen, or be burnt. They may be damaged by moisture or vermin, they may go out of style, or the price may decline. Owners incur these expenses and risks in the hope of making a

profit which is expected from an advance in the selling price while the goods are in storage.

Where should goods be stored? Goods may be stored at the point of production, at the point of consumption, or at an intermediate point through which they pass during the marketing process. In order to keep consumers supplied at all times, it is often necessary that some reserve stocks be kept near the points of consumption. In the past, seasonally produced farm crops have commonly been shipped soon after harvest, and thus a heavy, temporary burden has been placed on the railroads. It has been suggested that these goods should be stored for longer periods at the points of production in order to equalize the burden of the railroads. On the other hand, it has been contended that more coal should be shipped in the summer and stored near the consumers in order to equalize production and transportation.

Some of the factors to be considered in determining the best place to store goods are:

1. The keeping of necessary reserve stock near the consumers;
2. The equalization of the transportation burden on the carriers;
3. The location of the best physical storage facilities; such facilities can often be utilized more fully if provided in large market areas.
4. The place where money can be borrowed to best advantage to carry the goods while in storage;
5. Transportation facilities. Goods are often stored in terminals where they can be received and shipped easily. Goods may be stored in ports where they have to be transshipped from vessel to railroad or from railroad to vessel.
6. Freight rates. Other things being equal, goods should be stored where the transportation costs of getting them to the consumer will be least.

Freight rates are generally lower on carload lots than on less-than-carload shipments. For this reason, goods should ordinarily be shipped the maximum distance in carloads, which often means that they are shipped in carloads to points near the consumers. Here they are unloaded and stored ready for

shipment to the retailers by truck or by rail in less-than-carloads. There is need for considerable study in determining the proper locations for storage houses. Both transportation and storage costs should be held down. The seller with stocks within easy reach of the retailers has a strong selling advantage; at the same time, if he carries stocks at an unreasonably large number of points, storage costs will be excessively high.

This saving in freight rates by storing at central distributing points is illustrated by the shipment of catsup from New York to Rockford, Illinois. The retailer in Rockford does not need a carload of catsup at one time. If he has it shipped from New York in less-than-carloads, the freight will be, say, $1.59 per 100 pounds. The catsup, however, can be shipped to Chicago in carloads (36,000 lbs.) for 56½ cents per 100 pounds. The less-than-carload rate from Chicago to Rockford is, say, 45 cents. Thus the total cost of shipping in this way is $1.015 per 100 pounds. Here is a saving of 57½ cents, while the cost of storing in Chicago for one month is 12.8 cents.

In the past, the wholesaler was depended on to carry large stocks of goods. At present, however, many wholesalers carry relatively small stocks in order to reduce the cost and risks of storage. Manufacturers have often assumed a large part of the storage function. Improved transportation service during recent years, however, has lessened the need for carrying reserve stocks. Many manufacturers now carry small stocks, producing goods only as rapidly as they are sold or keeping only a little ahead of sales. This scheme gives the consumer fresher goods and reduces the costs and risk involved in storage.

Seasonally produced farm products must be stored until needed. The question often arises as to whether the farmer should sell his products as soon as they are harvested or whether he should store them for sale toward the end of the season. In some years the prices are much higher toward the end of the season than at harvest time, and profits are made by storing goods. In other years the spring prices are lower than in the fall, and losses result from storing goods. Several studies indicate that, over a period of years, Spring prices are about enough above Fall prices to cover the costs of storage: interest, rent,

handling, shrinkage, and deterioration. The inference is that if a farmer is able to study all supply and demand factors carefully he can decide at each harvest whether to sell his goods at once or store for a rise in prices. If he is not capable of making such forecasts, then he might just as well follow the practice of selling as soon as the goods are harvested.

Public warehouses. Warehouses are either public or private. Public warehouses are operated to store goods for the public for pay. There are six classes of public warehouses:

1. Merchandise, for the storage of general merchandise;
2. Household goods;
3. Cold storage, for the storing of goods that must be kept cold;
4. Special commodity, for storing particular types of goods, as grain, tobacco, or cotton;
5. Bonded, where goods can be stored under bond. This is necessary when the movement of goods is regulated by the government, as is the case with imported goods upon which the duty has not been paid.
6. Branch public or field. Goods are placed in the hands of a public warehouseman but are stored on the owner's premises. This procedure secures the advantages of storing in a public warehouse without incurring the expense of moving the goods from the owner's premises.

Services of public warehouses. There are several advantages of storing goods in public warehouses. A negotiable receipt may be obtained and used as collateral for loans from banks or finance companies. The goods cannot be removed and sold without the warehouse receipt, which is held by the creditor as collateral. The warehouse receipt is secured by a certain quantity of goods. While these are in the hands of the warehouseman, they cannot be levied upon by the creditors of their owner. Borrowing on a warehouse receipt reduces the amount of capital which is necessary to carry goods; conversely, the warehouse receipt enables an individual to carry a larger quantity of goods than he could with his own capital.

By storing in public warehouses, one need pay only for the actual amount of space used. Since the amount of space needed

often varies widely from one time to another, the seller who provides his own warehouses may have much idle space at certain seasons.

Many of the better public warehouses are well constructed; they are fireproof, equipped with automatic sprinklers, and are under guard 24 hours a day. For these reasons, insurance rates on goods in such houses are often much lower than for goods stored in poorly constructed or inadequately guarded private warehouses. The reduction in insurance rates is often a very worth-while saving. In some instances insurance rates savings as high as 90 per cent have been reported.

The public warehouse is especially adapted to the needs of a seller who wishes to carry regional stocks of goods but who does not have enough goods at the various depots to justify maintaining his own warehouses supervised by his own employees.

Public warehouses render other services for their patrons. They will (1) receive goods in carlots and ship them out in less-than-carlots; (2) pack or crate the goods when necessary; (3) issue invoices; and (4) ship goods on a C.O.D. basis or draw drafts to accompany shipments made on order bills of lading. Extra charges are made for such services.

Liability of public warehouses. Public warehousemen are liable for goods only when the goods are destroyed or damaged because of the operators' negligence. For this reason, goods in public warehouses are usually insured. The warehousemen must ordinarily return to the owner the identical goods placed in storage; an exception is made in the case of commodities such as grain, which may be mixed with other goods of the same grade. The warehouse must then deliver only the same quantity of the same grade. Goods which may be mixed with similar goods are known as fungible goods.

Charges of public warehouses. The public warehouse bases its charges on the space occupied by the goods, the length of time they are kept in storage, and the cost of moving them in and out of the storage warehouse. As mentioned above, extra charges are made for other services such as making shipments, packing goods, and making invoices.

In addition, extra charges, known as "modifications for cause,"

are made for goods that require unusual care or that must be stored under special conditions. Examples are furnished by silk, which has a very high value; by mirrors, which are very fragile; by beans, which are attractive to vermin; by onions and green hides, which are malodorous; and by liquids, which are subject to leakage.

General merchandise warehouses generally make a separate handling charge for moving goods in and out and a monthly charge for the time the goods are left in storage. Cold storage houses make a charge for the first month high enough to cover the cost of handling the goods; a lower charge is then made for each additional month.

Typical rates are:

COMMODITY	MERCHANDISE HOUSES[1]	
	Handling Charge In and Out	Monthly Storage Charge
Canned vegetables, per case (#2 size)...	.013	$1.40 per ton
Flour, per 100 lb. jute bag............	.033	$1.40 per ton
	COLD STORAGE HOUSES[2]	
	First Month's Charge	Each Additional Month's charge
Eggs, per case (30 dozen)............	10¢	7¢
Butter, per 100 pounds................	25¢	12½¢

[1] Chicago 1945 rates. Obtained from W. D. Leet, Pres., Allied Distribution, Inc.
[2] Detroit 1945 rates. Obtained from L. C. Hodaff, Gen. Mgr., Grand Trunk Warehouse and Cold Storage Co.

Government-licensed warehouses. The Federal Government licenses warehouses to store certain staple farm products such as grain, tobacco, cotton, wool, peanuts, broomcorn, and dried fruits. The warehouses are operated in accordance with rules established by the Government, and products stored in such houses are graded according to U.S. Government standards. Because the warehouse receipt covers a definite quantity of staple goods of known grade, the receipts issued by these warehouses are preferred collateral: banks will loan more on them than on ordinary warehouse receipts and may make loans at lower rates of interest. It is argued that the Government should extend the use of licensed warehouses to staple manufactured goods.

Other Physical Functions

Standardizing. The determination of specifications for quality is known as standardizing. Standards may be based on weight, physical structure, chemical content, size, sweetness, ripeness, soundness, strength, or moisture content. When goods are of known quality, they can be bought and sold by grade, name, or description. Standards facilitate the exchange of goods by saving the labor of repeated inspections.

Standard goods have a more definite value than non-standard goods and can be handled with less risk. Prices are more accurately known. Banks will loan more on the security of standard than on non-standard products. With standardization there is less room for puffing, boasting, or bragging by the sellers. Middlemen can handle standard goods on narrower margins than they can non-standard goods. Buyers can secure better values.

A standard product should be of a known quality no matter where it is produced or bought. For instance, No. 2 yellow corn, No. 3 soft winter wheat, fancy yellow cling canned peaches, and size 2 ex-standard canned peas should be of a known quality, regardless of who the producer is. This fact suggests the need of uniform standards which may be set up by custom, by trade associations, or by Government agencies.

Some argue that lack of standardization is responsible for one of the largest wastes in distribution, a waste which runs into billions of dollars annually. According to this argument, small buyers, especially the consumers, are consistently overcharged because of their ignorance of quality. Instances are cited of relatively simple products that are sold by advertising and "high-pressure" methods for several times their cost. The list includes medicines, insecticides, cleansers, foods, pens, clothing, office supplies—in fact, practically all types of articles.

Corporations that purchase in large lots often set up their own testing laboratories and buy at prices much lower than those charged to buyers less fortunately situated. It is argued that huge sums could be saved if definite standards were drawn up and all producers were required to label their products with

the proper grades. It would then be possible for the consumers to recognize the grade they wanted and to buy this grade from the seller at the lowest price. Competition would be placed on a price basis, and large expenditures for advertising and salesmanship would be greatly reduced.

Thus runs the argument, and there appears to be considerable truth in it. Opportunities for large savings are possible, even though all the savings claimed might not be realized. Not all products can be standardized; some are bought for their individuality. Producers who make goods of various styles, colors, and flavors would be likely to advertise their goods as having better or more distinctive qualities. It would take several years and considerable expense to educate the great majority of the people to purchase by grade.

Standardization should be encouraged, however, although all the advantages claimed by its advocates may not be realized.

Grading. Closely associated with standardizing is grading. They are often considered as two aspects of the same function. Standardizing is the setting up of rules or specifications, and grading is the application of these rules: the physical work of inspecting, testing, or sorting goods in accordance with the specifications.

Assembling. The bringing together of similar goods to obtain larger quantities for shipment or sale is called assembling. The country grain elevator collects and stores wheat in quantities large enough for carload shipments. The cotton merchant brings together enough cotton to be able to supply the mills with large lots of uniform quality. Assembling is important for goods such as farm products which are produced in small quantities in scattered locations.

Dividing. The separation of goods into smaller lots for sale is called dividing. To illustrate, the wholesaler receives a carload of eggs, and since the ordinary retailer cannot use a carload at one time, the wholesaler divides the load and sells it to retailers by the case. The ordinary consumer does not want a case of eggs at one time; hence the retailer divides the case and sells the eggs to consumers by the dozen.

Dividing should not be confused with grading. Goods may

be separated in grading, but this separation is done on the basis of quality. In dividing, goods are sorted not according to quality but merely to provide the conveniently small lots desired by the buyers.

Packing. Goods are packed for transportation and storage so that they can be handled and protected from damage or loss. They may be wrapped, crated, or placed in bags, bottles, barrels, or other containers. Liquids require leak-proof containers. Fragile goods must be packed with particular care or placed in special containers.

Questions

1. What are the principal physical functions performed in the handling of goods?
2. What utilities does transportation create?
3. What is the relationship of transportation to the development of markets?
4. What is a common carrier? What is the liability of a common carrier?
5. Distinguish between a straight bill of lading and an order bill of lading.
6. Define or explain the following: demurrage, diversion, reconsignment, in-transit privileges.
7. What is the place of the motor truck in the transportation system? Is the relative importance of the motor truck likely to increase?
8. What are some of the influences of the passenger automobile on marketing?
9. What utility does storage create?
10. What influence may the storage of commodities have on price?
11. Some farmers believe that storage reduces the prices which they receive, by increasing the supply of goods on the market. Do you agree? Explain.
12. Against what risks do adequate storage facilities protect?
13. What effect may quick freezing have on (a) marketing? (b) the establishment of cold storage plants? (c) locker plants?
14. What costs or expenses are involved in storage?
15. What factors should be considered by a manufacturer in determining where to store goods which are distributed to retailers?
16. What is a public warehouse?
17. What services are performed by public warehouses?
18. What is the liability of a public warehouseman?

19. What are the bases for the rates charged by public warehousemen?
20. Does insurance reduce the cost of storage?
21. Will improved methods of production and transportation make it unnecessary to store goods for long periods?
22. Distinguish clearly between standardizing and grading.
23. What are the wastes which result from the lack of generally accepted standards?
24. Should the Federal Government take steps to establish and to bring about the acceptance of standards for consumer goods?
25. Define or explain the following: assembling, dividing, packing.
26. Would the establishment of standards by the Government, and the requirement that all sellers label their goods with the established standard, reduce economic wastes? Would you say that the following are standard products: Heinz baked beans? Listerine shaving cream? Gillette razors? No. 2 red winter wheat? Sunkist oranges?
27. We spend much effort and money to reduce transportation costs. Then we enact high tariffs to make it more expensive to take goods from one country to another. Can you explain this inconsistency?
28. What suggestions can you make for improving railroad freight service?
29. Should motor trucks be taxed enough to cover their share of the costs of building and maintaining the highways and streets? Are they so taxed in your state?
30. Who should pay the cost of improving and maintaining our inland waterways (including the cost of building and operating necessary locks)? How should the money be collected?
31. What do you think of the future of air transportation?
32. As a manufacturer of nationally distributed goods, how would you go about determining at what points you should carry stocks of goods for distribution to retailers?
33. What advantages would follow the establishment of Government-licensed warehouses for manufactured goods? It has been said that the Government is unfair in establishing such warehouses for farm products and not for manufactured products. Do you agree?
34. Does insurance reduce marketing costs? Would it be desirable for the businessman to shift all possible risks to insurance companies? Why or why not?

3

Middlemen, Trade Channels, and Commodities

In this chapter the relationship of middlemen, goods, and functions will be discussed. This is done to provide the reader with a broad picture of marketing before taking up the subject further in detail.

The Middleman

The study of middlemen (or market institutions) shows what goods the middlemen handle and what services (functions) they perform. This approach is a practical method of studying market distribution. It shows how these middlemen conduct their operations and thus is helpful to men engaged in marketing.

There are many types of middlemen: wholesalers, jobbers, brokers, sales agents, commission merchants, milk dealers, coal dealers, lumber yards, terminal elevators, filling station operators, garages, cotton buyers, tobacco and fruit auctions, grain elevators, live stock shippers, farmers' coöperative associations, mail-order houses, chain stores, department stores, general stores, drugstores, hucksters, neighborhood stores, cigar stands, ice cream parlors, restaurants, soda fountains, newsstands, florist shops, and so on. In order to study middlemen, it is desirable that they be grouped or classified in some way.

Kinds of middlemen. Those individuals, partnerships, and corporations engaged in marketing are known as middlemen. When classified on the basis of ownership, there are two principal kinds or classes of middlemen: First, those who own the

goods—that is, have legal title to them. These middlemen are merchants in that they buy and sell goods in an attempt to make a profit. In addition to other marketing functions, they assume the risks involved in the ownership of goods. Second, those who are agents—who do not own the goods but perform certain marketing functions for pay. These are called *functional* middlemen for the reason that they perform marketing functions without assuming the risks of ownership.

Merchants. There are many types of merchants. We may group them broadly into three main groups: country shippers, wholesalers, and retailers.

The country shipper is engaged in buying farm products, assembling them at country points, and shipping them to central markets. Country grain elevators and warehouses, livestock buyers, specialized produce dealers, creameries and cream stations, and cotton buyers are examples of country shippers. These are discussed in Chapters 8, 9 and 10.

Wholesalers are merchants who buy goods and sell to other merchants and to manufacturers. They operate between country shippers and manufacturers on one side, and retailers and industrial buyers on the other side; they do not sell to the final consumers. There are many types of wholesalers. Some have warehouses and others handle goods in railroad cars or public warehouses. Some wholesalers have organizations of traveling salesmen and make deliveries to the buyers; others operate on the cash-carry basis. Some wholesalers are privately owned and operated for profit; others are owned by retailers. Some wholesalers handle full lines of goods, and others handle only a few items. Some handle industrial equipment and sell to industrial buyers, while others handle consumption goods and sell to retail dealers.

The retailer is the middleman who sells direct to the household consumer. He is the most familiar type of middleman. There are many types of retailers: chain stores, department stores, newsstands, mail-order houses, lunch rooms, restaurants, coal yards, soda fountains, neighborhood stores, stores handling shopping lines, and stores handling convenience goods.

Retail stores may be classified in many ways, but for our

purpose we shall classify them as individual or unit stores, department stores, mail-order houses, chain stores, wagon retailers, and bulk retailers.

Functional middlemen. The functional middleman is an agent who performs certain definite marketing functions for pay without owning the goods—that is, without having title tc them. He works for definite pay and does not buy and sell foı profit. Such middlemen may be grouped according to the func tions performed. A partial list follows:

Buying—purchasing agents, brokers, resident buyers.
Selling—brokers, sales agents, commission merchants, selling houses, manufacturers' agents, auctioneers, advertising agencies, market counsellors, and market research agencies. Few of these agents perform all divisions of the selling function.
Transportation—railroads, trucking companies, steamship companies; electric railways; air transport companies; package delivery companies.
Storage—public warehousemen; commission merchants.
Grading—licensed inspectors, commission merchants, testing laboratories, appraisers.
Dividing—commission merchants, public warehousemen.
Financing—finance, credit, and discount companies; banks; sales agents; collection agencies; factors or commission merchants.
Risking—insurance companies.
Recording—public accountants, market research agencies.

The operations of common carriers and public warehouses have already been discussed in describing the transporting and storing functions. The operations of brokers, sales agents, and commission merchants are described in the next chapter.

Trade Channels

Goods ordinarily pass through the hands of one or more middlemen between the producer and the consumer. The trade channel is made up of the middlemen who handle an article on its way to the consumer. We may include in the trade channel only the merchants who have title to the goods, or we may include, in addition to these, all those who perform any marketing function. If the latter course is followed, we would include the physical movements of the goods by railroads,

truckmen, warehousemen, and others; financing of goods by banks and finance companies; assuring of risk by insurance companies; storing goods by warehouse; and so on for all other marketing functions. This would give longer and more complicated channels. We are ordinarily more interested in following the ownership of the goods rather than their physical movement, and we shall therefore think of the trade channel as composed of only those middlemen who buy and sell, regardless of whether they are the owners of the goods or whether they act as agents for the owners.

Manufactured goods. We may follow the trade channel of an article from the producer of the raw material through the various middlemen and manufacturers to the consumer of the final product. This often makes very long and complicated trade channels, as many products go through several manufacturing processes. Often a single raw material makes several products, while in other cases it takes several raw materials to make one finished product. For these reasons it is simpler to consider that a trade channel extends from the producer of an article to the consumer of this article, whether the consumer be the manufacturer or the household consumer of the final product. Thus the trade channel for wheat extends from the farmer to the flour mill, while the trade channel for flour extends from the flour mill to the baker, and the channel for bread extends from the baker to the final consumer. There is thus one trade channel for wheat, another for flour, and a third for bread.

Trade channels illustrated. The shortest possible trade channel is found when the producer of goods sells them to the consumer—for example, when a farmer sells his goods to the consumer. Goods, however, commonly pass through the hands of one, two, three, four, or more middlemen.

Only one middleman may be included when the farmer sells his eggs to the retailer or when the manufacturer sells his shoes to the shoe dealer. Manufacturers often sell to wholesalers who sell to retailers. This trade channel involves two middlemen, the wholesaler and the retailer. This channel is followed by many manufactured products.

$$\text{Producer}\rightarrow\left\{\begin{array}{l}\text{Wholesaler}\\ \text{Chain-store warehouse}\\ \text{Commission merchant}\\ \text{Mfr's branch house}\\ \text{Broker or sales agent}\end{array}\right\}\begin{array}{l}\rightarrow\text{Retailer}\rightarrow\text{Household Consumer}\\ \\ \rightarrow\text{Wholesaler}\rightarrow\text{Industrial Consumer}\\ \quad\text{or supply house}\end{array}$$

The manufacturer, however, often reaches the wholesaler through a broker, which involves three middlemen: broker, wholesaler, and retailer.

$$\text{Producer}\rightarrow\left\{\begin{array}{l}\text{Broker}\\ \text{Sales agent}\\ \text{Buying agent}\\ \text{Local buyer}\end{array}\right\}\rightarrow\begin{array}{l}\text{Wholesaler}\\ \text{or jobber}\end{array}\rightarrow\text{Retailer}\rightarrow\text{Consumer}$$

Four middlemen are involved in the sale of many farm products. These middlemen may be a country shipper; a commission man or broker; a wholesaler or jobber; and a retailer.

$$\text{Producer}\rightarrow\left\{\begin{array}{l}\begin{array}{l}\text{Local}\\ \text{buyer}\end{array}\rightarrow\left\}\begin{array}{l}\text{Broker}\\ \text{Auction}\\ \text{Com. mer.}\\ \text{Wholesaler}\end{array}\right\}\rightarrow\text{Jobber}\rightarrow\text{Retailer}\rightarrow\text{Consumer}\\ \text{Sales agent}\rightarrow\text{Broker}\longrightarrow\text{Wholesaler}\rightarrow\text{Retailer}\rightarrow\text{Consumer}\\ \text{Importer}\rightarrow\text{Broker}\longrightarrow\text{Wholesaler}\rightarrow\text{Retailer}\rightarrow\text{Consumer}\end{array}\right.$$

Imported goods may pass through the hands of the importer, broker, wholesaler, and retailer, in addition to middlemen in the exporting countries. Longer trade channels than these are not unusual. Eggs, for example, may be handled by two or three middlemen in the country and three or four middlemen in the city markets.

Factors determining the trade channel. Some of the factors that determine the channel a product follows are: distance between producer and consumer; perishability of product; number of products sold by the seller; scale of production, that is, whether the goods are produced on a small or large scale; scale of consumption; financial position and size of seller; and the need for special facilities for handling the product.

The greater the distance between producer and consumer, the longer the trade channel is likely to be. A highly perishable product must be marketed quickly, and may hence have a shorter trade channel than a nonperishable product. Manufacturers of ice cream and bread, for example, usually sell either

to the retailers or to the consumers. The manufacturer of a large number of products is likely to carry the product nearer to the consumer than is the manufacturer of a single product.

Goods produced on a small scale, like farm products, must be assembled. This often increases the length of the trade channel. Large or well-financed sellers may perform more of the marketing functions and carry the goods further along the trade channel than smaller concerns.

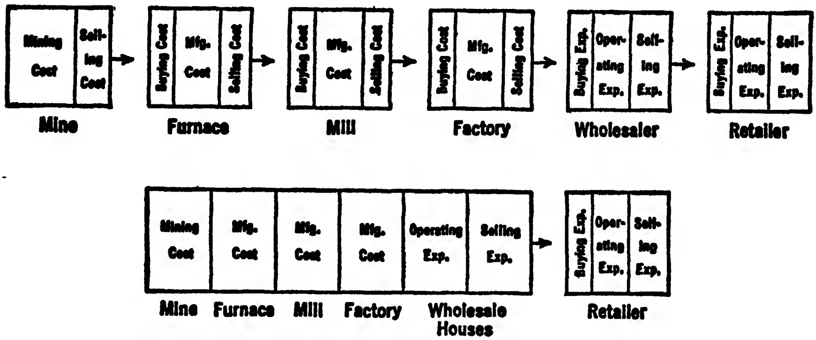
When goods need special facilities for handling, the seller must either provide and operate these facilities or sell through middlemen who provide them. Very often these facilities are supplied by the manufacturer. Gasoline must be stored in tanks and delivered to the retailers in tank trucks. The oil refiners commonly provide these facilities and perform the wholesale functions. Fresh meat must be kept in cold storage warehouses; many of these are provided by meat packers, who handle the meat until it reaches the retailers.

Sale in same stage of distribution. Sales are often made in the same stage of distribution, that is, between similar middlemen who perform the same functions. Such sales do not pass the goods on toward the consumer and are frequently made for speculative purposes. By this is meant that the buyers attempt to make a profit out of a change in price and not by performing a service. Such speculative sales are ordinarily condemned, although it is argued by some that they tend to stabilize prices.

There are sales in the same stage of distribution that do not involve speculation, as when one dealer overbuys and another underbuys. To illustrate, we shall assume that a wholesaler estimates that during a season he will sell 3,000 cases of peaches and buys this quantity. His sales are less than expected, and toward the end of the season he finds that he is overstocked. He notifies a broker who finds another wholesaler who needs the peaches and makes the sale. The peaches are still in the same stage of distribution, and no closer to the consumer than when they were in the hands of the first wholesaler. Yet the sale resulted from misjudgment and not speculation. If, on the other hand, the wholesaler had bought more peaches than he expected to sell to his customers because of an expected ad-

vance in price, he would have been a speculator on the extra peaches.

Integration. Integration means the operation of successive steps, or stages, in the production or marketing of goods, by one concern. In regard to marketing, we think of an integrated concern as operating the machinery for carrying the goods through two or more stages of distribution.[1] Thus the manu-



The advantages of integration. Chart showing how the trade channel is simplified and how successive buying and selling expenses are eliminated by integration. *Above*—trade channel without integration; *below*—trade channel of a concern integrated from the production of raw material to the retailer.

facturer who sells to the retailers is integrated in that he performs the wholesale functions in addition to the manufacturing functions. The chain store is integrated in that it operates both wholesale warehouses and retail stores. Many manufacturers are integrated and operate both factories and wholesale stores.

Integrated concerns have two important advantages: First, they eliminate the cost of buying and selling goods between the different parts of the organization. Thus in an integrated industrial concern, the mine does not have to sell to the furnace, the furnace does not have to sell to the rolling mill, the rolling

[1] This is called vertical integration. Some call the consolidation of similar concerns horizontal integration. Thus if several steel mills combine, the consolidated company is said to be horizontally integrated. The consolidated concern may make some savings by reducing the number of salesmen and the amount spent for advertising. Such savings, however, are not always realized. These concerns may attempt to control prices, for which reason they are often frowned upon by consumers and the Government.

mill needs no salesmen to sell to the foundry, and so on with successive manufacturing stages. Similarly, the chain store needs no salesmen to sell to its retail stores, and the retail store managers spend little time interviewing salesmen, as they requisition most of their goods from their warehouses.

Second, risk is reduced as markets are more definitely assured. This enables operations to be planned with greater assurance and the plants to be operated more evenly. Mines owned by an integrated concern know that they have an outlet for their products so long as the factories operate. The wholesale houses of chain stores buy with assurance, knowing that they have a definite demand from their retail stores.

Limitations on integration. In order to secure the full advantage of integration, the various parts of a concern must be co-ordinated. Suppose a department store operates a blanket factory. There is no cost in selling the blankets to the department store. If, however, the store is unable to sell all the blankets made by the mill, selling expense is incurred in selling the remaining blankets. Again, an integrated concern may be poorly managed because of the variety of its operations. The hired manager of the department store's blanket mill may be less efficient than the owner of a similar mill whose organization is devoted entirely to the operation of the mill.

Types of Goods

Goods may be divided into industrial goods which are used in further production, and consumer goods which are ready for sale to the household or ultimate consumer.

Industrial goods. The manufacturer of industrial goods is likely to have his own sales organization and sell direct to industrial buyers for two reasons: sales are usually made in large units so that direct selling is economical; and many of these products are technical in nature and require specially trained salesmen. Frequently equipment is made to suit the needs of the individual buyer, and requires salesmen with engineering, metallurgy, chemistry, or mechanical training in order to sell it. For raw materials such as rayon, steel, and chemicals the

salesmen need a specialized knowledge of uses in order to sell the products best suited to the needs of the buyer. When salesmen with highly specialized knowledge and training are required, the manufacturer usually directs his own sales organization so that he can train and supervise his salesmen and maintain direct contact with the users.

However, many industrial goods are also sold by manufacturers' agents and wholesalers. The manufacturers' agent selling machinery or raw materials may have skilled salesmen. Since he represents several manufacturers, his services may be used by small manufacturers who cannot afford large sales organizations. Agents are also useful as scouts to locate prospective buyers, because they contact many factories and learn when new machines are wanted or when new plants are to be erected. They may take the initial steps in developing sales; the manufacturer then sends his own salesman to help in the final stages.

Wholesalers also sell to small buyers and to those buyers who want immediate delivery. Steel jobbers, for example, carry stocks and sell in smaller quantities than the large mills. They are useful in selling to less-than-carload buyers and to contractors and factories who need small lots of steel immediately. Mill supply houses, machinery distributors, hardware jobbers, and electrical goods wholesalers are important in the sale of industrial goods, especially smaller pieces of equipment and machinery, repair parts, and the like.

Consumer goods. The three main types of consumer goods are shopping goods, convenience goods, and bulk goods.

Shopping goods are goods of distinctiveness or high unit value. They are of such importance to the consumer that he will spend considerable time in their selection. They are not purchased every day and the consumer is often willing to travel fairly long distances to secure the desired goods. Goods of high unit value are automobiles, refrigerators, washing machines, men's suits and overcoats, women's coats, furniture, rugs, watches, sets of silverware, dishes and similar items. Goods wanted for their fashion element or distinctiveness in-

clude dresses, women's hats, gift articles, curtains and draperies, art goods, and many others. Many articles have both qualities: high unit value and distinctiveness.

Shopping goods are divided into two classes: fashion goods and service goods. Fashion goods are purchased for their style qualities or distinctiveness. Their purchase is concentrated largely in shopping or trading centers. These are the downtown and outlying shopping centers in our large metropolitan areas, and in trading center towns throughout the country. Trading centers are of two kinds, primary and secondary. Primary trading centers are towns or cities with stores selling fairly large assortments of furniture, home furnishings, and wearing apparel for men, women, and children. They usually have several stores selling each type of goods and at least some of the stores handle high quality merchandise. Primary trading centers usually are located in towns of over 10,000 population,[2] although in the less densely populated areas, some towns of less than 10,000 population may be primary trading centers. In our 3,072 counties there are about 1,200 primary trading centers where most fashion goods are sold.

Towns of between 1,500 and 10,000 population are usually secondary trading centers. The stores sell some lower-priced clothing and furniture but relatively few high-quality goods in these lines. Secondary trading centers are important in the sale of convenience, bulk, and service goods.

Service goods are durable goods of high unit value which require service in repair, delivery, installation, or credit. Typical service goods are automobiles, refrigerators and other home appliances, and farm equipment. Since mechanical performance is of more importance than style in service goods, the consumer prefers to buy such goods from nearby dealers who give good repair service. Large assortments are of less importance than with fashion goods and the small town dealer has or can secure all the models available to the city dealer. Service goods are sold chiefly by dealers in the outlying shopping and

[2] Some suburban and satellite industrial and residential towns of this size are only secondary shopping centers and not primary trading centers.

neighborhood retail districts of large cities, in primary trading centers, and in secondary trading centers. The latter are relatively important.

Convenience goods are goods of small unit value for which consumers do not shop; instead they are purchased at the most convenient places: grocery, drug, and hardware stores, filling stations, restaurants, and newsstands. Convenience goods are usually of standard or known quality. They may be goods needed in emergencies or perishables which must be bought in small quantities. Some are goods bought on the impulse of the moment. Typical convenience goods are foods, drugs, toilet articles, gasoline, newspapers, magazines, candy, cigarettes, and household supplies such as light bulbs, soap, screen wire, or nails.

Convenience goods are sold by stores located in the neighborhood retail districts of large cities, in suburban towns, in primary and secondary trading centers, in small village and crossroads stores, along our highways, in the downtown business districts of our large cities, in lobbies of hotels and office buildings, on street corners, and in railroad and bus stations. In short, wherever people live, work, or travel.

Bulk goods consist of heavy goods that must be delivered. Coal, fuel oil, lumber, brick, cement, gravel, and stock feeds are examples. They are sold principally by retailers who are located on rail sidings and who have equipment to handle and deliver bulk products. Because of the expense of delivery most bulk goods are purchased near where they are used. Consequently small town and neighborhood retailers are important in distributing such goods.

Influence of type of goods on choice of outlets. The manufacturer, when selecting his method of distribution, should consider first the type of goods. If his product is a convenience item, he wants it handled by the largest possible number of retailers. To reach the thousands of widely scattered small stores in neighborhoods and villages requires a large sales organization. The manufacturer of convenience goods will likely sell to wholesalers unless he has a long enough line to enable him to develop a chain of wholesale houses as the meat packers have

done. If he makes fashion goods, however, he is much more likely to sell direct to the retailers, most of whom are located in the shopping districts of the larger cities and other primary trading centers. A smaller sales organization is needed than that required to sell convenience goods. There are, for example, some ten times as many stores selling food as women's clothing. The stores selling fashion goods are usually larger than those selling convenience goods.

Since fashion goods have a high value per pound, the wholesaler's service in making carlot purchases and securing carlot freight rates to nearby warehouses is not necessary. Fashion goods should reach the retailers quickly before they go out of style. Storage in wholesale houses causes delay, hence such goods are seldom handled by wholesalers. Wholesalers in the fashion goods trades handle principally the more staple or lower-priced merchandise. They sell mainly to the smaller dealers, especially those located in the secondary trading centers.

Furniture is a fashion good but styles in furniture do not change as rapidly as in many other goods. Because furniture is bulky, handling through a wholesale house would be expensive; most furniture stores therefore buy direct from the manufacturer in fairly large quantities. Retailers place large orders when they visit the various furniture shows or exhibitions sponsored by manufacturers in Chicago, Grand Rapids, High Point, Jamestown, and San Francisco.

Perishability shortens the trade channel for such products as bread, cake, pie, ice cream, potato chips, and newspapers. These are usually made locally and sold direct to retailers or consumers. Gas and electricity are usually sold direct to consumers owing to the necessity of special facilities for their delivery.

Service goods are usually handled through manufacturers' branch houses or by wholesalers, often called "distributors."

Bulk goods are commonly shipped direct to retailers or industrial users in carlots and are not ordinarily handled physically by wholesalers except where they are transshipped from rail to water or water to rail. However, many are sold by drop shippers.

Specialties are not listed as a separate class of goods. The concept of a specialty is, however, often used in marketing. The word "specialty" has several meanings but usually connotes a distinctive product, an item that is different from others, one that is the opposite of a staple product. It may be a new product that is not in general use or a product of distinctive design. A specialty may be an article for a special or limited use or one that appeals to a limited number of consumers. As there is no other product just like it (at least in the opinion of the manufacturer), a specialty is not in direct price competition with other goods. Therefore it often carries a wide margin and may be highly profitable if it can be sold in quantity.

The word "specialty" is also used to denote one product as opposed to a full line or family of products. Thus, a specialty manufacturer makes only one or a very few products. A specialty salesman sells the goods of only one producer in contrast to the jobber's salesman who sells the goods of many manufacturers.

A specialty may require special promotion by salesmen, advertising, or both. It may be sold direct to consumers or to retailers who will devote special attention to its sale. The periodicals in which it is advertised should be selected with great care.

Classification of a product changes. A product may not remain permanently in the same class. A product may at one time be a specialty, and at another a staple. A product may be a fashion good at one time and later a convenience good. To illustrate, until fifty years ago silk hosiery was a specialty. Later it became a high quality fashion good, then a low fashion good, and when it went off the market during the War, it was on the border between a fashion and a convenience good. Toothpaste, to take another example, was formerly a specialty as people had to be educated to its use. Now that most people clean their teeth it is a convenience good sold principally by drugstores. Toothpaste is so generally used that it would seem that it should be sold in grocery stores because they operate on lower margins and could sell it at lower prices.

Much waste occurs because sellers do not quickly realize that

their products have moved from one class into another. For example, a product is new and must be sold as a specialty. It requires skilled salesmen who are paid high salaries. Later it wins general acceptance by the consumers. High grade salesmen are no longer needed and should be replaced by the order-taker type of salesmen whose job is to see that wholesalers and retailers are kept fully stocked.

Farm products. These are partly industrial raw materials and partly consumer goods. Logically, farm products might be discussed under these two classifications. There are, however, some problems peculiar to the marketing of farm products regardless of whether they are raw materials or ready for home use as they leave the farm.

The chief characteristic of farm products from a marketing standpoint is that they are produced on a small scale and must be concentrated to supply manufacturers or large markets. This gives rise to a large group of middlemen, constituting the general class of "assemblers of farm products." In this class are grain elevators, livestock buyers, cream stations, farmers' co-operative associations, fruit and vegetable buyers, milk dealers, tobacco and other country auctions, and some types of brokers and commission merchants. Country stores often assemble farm products, particularly eggs, cotton, and cream. After farm products are assembled at rural points, they pass through regular trade channels to factories or city markets.

Most farm products are raw materials and must be manufactured before they are ready for consumption. In this class are wheat, flax, soybeans, livestock, cotton, tobacco, broomcorn, wool, sugar beets and sugar cane, vegetables and fruits for canning, tung nuts, rubber, a large amount of corn, milk for manufacture into butter or cheese, and, if pasteurization be considered as manufacturing, milk for fluid consumption. Some farm products are consumer goods—fresh fruits and vegetables, eggs, home-killed meat, farm butter, nuts, live poultry, and raw milk.

Organization of material. We shall consider the operation of various types of wholesale middlemen in the following chapters. More attention will be given to middlemen engaged in

the distribution of consumer goods than to those who handl industrial goods. However, many dealers handle both classes o goods. The student should keep the classification of commodi ties constantly in mind while considering the operations of th various middlemen.

Following the chapters on wholesale middlemen and th choice of a trade channel by the manufacturer, we shall discus the distribution of industrial goods and farm products. Th distribution of these commodities differs in many importan respects from the marketing of consumers' goods.

Questions

1. What is meant by the middleman approach to the study o marketing?
2. Name different types of merchants.
3. Define functional middlemen.
4. What are country shippers? What functions do they perform?
5. Name types of wholesalers and retailers.
6. Name different types of functional middlemen.
7. What is meant by a trade channel?
8. Give illustrations of trade channels involving one, two, three and four middlemen.
9. What factors determine the trade channel followed by differen products?
10. Should we attempt to make one trade channel include the marketing of products all the way from the producer of the raw material to the consumer of the finished product?
11. What is meant by a stage of distribution?
12. Why are goods sold in the same stage of distribution?
13. What is meant by integration?
14. What are the advantages of integration? How may it reduce marketing costs?
15. What are the limitations on integration?
16. Distinguish vertical and horizontal integration.
17. A wholesale dry goods house operates mills producing cotton cloth, towels, sheets, sweaters, blankets, cotton and rayon hosiery, and house dresses. It normally sells to retailers the entire output of the plants making towels, sheets, hosiery, and house dresses. A considerable portion of the outputs of the other plants must, however, be sold to other wholesalers, chain stores, and other large buyers.

   (*a*) Is this concern integrated? Is marketing cost reduced by

the ownership of the factories? Do you believe that this wholesale house can operate these various factories as efficiently as they could be operated by independent companies?

(b) This wholesale house decides to open a chain of retail stores. The chain can be supplied very largely from the wholesale house and will help to utilize the outputs of all the factories. Will the establishment of this chain of stores enable goods to be marketed more cheaply than when the wholesaler sold to independent retailers? Will the consumer be benefited?

18. What are the three main types of consumer goods? Describe each type.
19. What types of goods are the following: locomotives; ice; men's work shoes; women's dress shoes; overalls; filing cabinets; washing machines; coal bought by a factory; coal bought by an individual consumer; pig iron; iron ore; cotton; corn for manufacture into cornstarch; sugar for manufacture into candy; silk hosiery; men's suits; women's silk dresses; typewriters; cigarettes; milk; butter?
20. How does the type of goods influence the type of outlet chosen by a manufacturer?
21. Why is the manufacturer of industrial goods likely to sell direct to industrial buyers?
22. What is a specialty?
23. Illustrate how a product may move from one classification to another. How does this affect the choice of outlet?
24. What are the characteristics of farm products from a marketing standpoint?

4

The Consumer

ALL MARKETING activity is directed at the consumer. Goods are produced for consumption, and all legitimate business organizations operate solely to supply the consumer's needs. It can be said that all marketing activities of manufacturers, wholesalers, and retailers should start with a study of the consumer and his wants and desires. How many consumers are there? Where do they live? How much money do they have? What are their wants? How are their wants going to change in the future? A study of the consumer leads to a study of our population and its probable growth or decline; a study of income and its distribution; and a study on consumer expenditures.

Population

The 1940 population was 131,700,000. This has increased to an estimated 139,000,000 at this writing and will probably be over 151,000,000 in 1960.[1] About 70 per cent of the population lives east of the Mississippi River and the highest density is along the north Atlantic Coast and around the southern shores of the Great Lakes.

Movement toward the cities. In 1900, three fifths of the

[1] The actual number is somewhat larger owing to under-enumeration by the Census Bureau. The actual population was estimated as 132,500,000 in 1940 and is predicted to be 144,700,000 in 1950. Thompson, Warren S., and Whelpton, P. K., *Estimates of Future Population in the United States,* National Resources Planning Board, 1943.

people lived in the country or in villages of less than 2,500 population. At the present time almost three fifths of the people live in cities and towns, one fifth on farms, and the other one fifth live in the country but not on farms ("rural-non-farm"). Almost one fourth of the total population lives in cities of over 250,000 population.

Two trends in these population shifts are important. First is the decrease in the proportion of the population engaged in farming. Only a few decades ago one half of our population lived on farms. Today one fifth of the population are farmers and this proportion may decline in the future. The use of machinery and other labor saving devices enables fewer workers to produce our food and other farm products. The second trend has been a movement of urban workers to the country, a movement made possible by the automobile. Some of these people live in the country so that they can raise part of their food, others because they like to live outside the towns where they work.

The development of an economic life characterized by a high degree of division of labor and specialization of work has been a continuous one for a century. The more one group of people depends on another, the larger the market becomes. The improvement in production techniques bids fair to continue indefinitely, so in all likelihood, markets will continue to grow.

Birth and death rates. A characteristic of western industrialized civilizations is a declining birthrate. In the United States the birthrate declined from 25 per 1,000 population in 1915 to 16.6 in 1933, at the bottom of a severe depression. From this point it increased to 17.3 in 1939, and with the War to 21.5 in 1943 and the higher birth rate continued into the postwar business boom.[4] Some students predict that it will again decline when the effects of the War have worn off and the country is less prosperous. Even so the population will continue to grow for several decades but at a decreasing rate.

With purer water and milk supplies, less strenuous outdoor work, and better care of health, the death rate declined from 14.7 per 1000 people in 1910 to 10.9 in 1943. The declining death rate means that people live longer. According to the

American Medical Association, life expectancy has increased from 49.2 years in 1900 to 67 years in 1947. The proportion of old people in our population has increased and will probably continue to do so. In 1940, 12.4 per cent of the population was over 60 years of age. By 1960, the proportion is expected to increase to 13.1 per cent.[2] This fact is important to the seller, as old and young people have different wants.

The large number of births means an ever changing market. People are not born with a knowledge of and demand for any particular goods or brands of goods. There are some 2.5 million people born every year. In ten years there are 25,000,000 new consumers. Will these be won by established products and brands or will they buy new products?

The family. The family is the most important consuming unit. The great bulk of food, furniture, household appliances and furnishings as well as much of the clothing and entertainment is bought for family rather than individual use. Sellers of houses, and home equipment and furnishings of all kinds are interested in the number of families rather than the number of people. There were 35,000,000 families in 1940 and close to 39,000,000 at this writing. In addition to these families there are a number of people living outside family groups in rooming and boarding houses, private homes, hotels, clubs, camps, and vessel crews. The majority of these are younger persons who have left their parental homes and who have not yet set up homes of their own. There are some seven or eight million such persons. The majority of these people are employed and have their own incomes. As they are not operating homes they spend relatively little on furniture and home furnishings and relatively more on clothing and amusements. As the majority of these are young people who have not reached their maximum earning capacity, their average income is considerably less than that of families.[3] The number of families plus the number of individuals living outside of family groups makes up the number of *consumer* units.

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[2] Dewhurst, J. Frederic, *America's Needs and Resources.* The Twentieth Century Fund, 1947.

[3] There are also about a million and a half people living in institutions. These consumers are not buyers in the market as are most other people.

Families are of various sizes from one up to 10 or more. In 1940, 10 per cent of the families consisted of one person, 65 per cent of from 2 to 4 persons, and 25 per cent of more than 4 persons. Omitting one-person families, the average family consisted of 4 people. The average size of the family has been declining and apparently will continue to do so. It has been pointed out that even if the population stops growing, the number of families might keep on increasing for a considerable time. This increase in the number of families is important to sellers of furniture, stoves, refrigerators, radios, and other things used in the home.

Employment. It is estimated that there are approximately 60,000,000 people employed in the United States. There are less than 40,000,000 families. There are many families with no member gainfully employed—and some families are retired, ill or live off investments, pensions, or annuities. Deducting these and allowing for the number of employed single persons who live outside family groups and of one-person families, there are approximately 1.5 employed persons in the other families. Considering all families, the average is over 1.3 persons employed per family. This means that on the average a family has the income from one and a third workers. It is important in wage negotiations to determine what income per worker is necessary to support a family at a given scale of living.

The larger number of workers per family is largely accounted for by the increased number of women employed outside the home. In 1870, for example, 15 per cent of gainfully employed persons were women while in 1940, 25 per cent of the labor force consisted of women. The percentage of married women employed increased from 15 per cent in 1900 to 30 per cent in 1940. The employment of married women influences demand in several ways. It increases the demand for prepared and cooked foods which are either ready to serve or require little cooking. It increases the demand for ready-made garments particularly for women and children. Smaller families and the employment of married women give a demand for small apartments and houses equipped with various labor-saving devices.

Income

A market is composed of people with income and an inclination to buy. Income consists of money and goods received by others, of goods and services produced by the consumers; and of the use of durable goods (houses, automobiles, and furniture, for example) owned by the consumers. In the past most of the available figures have included only money income. The United States Department of Commerce, however, has revised its estimate of national income to include the rental value of owner-occupied houses.[4] This is an important addition. The home owner has more money to spend for other things than does the family with the same money income which must pay rent on its home. If a family raises its own vegetables it will spend less on food and more for other things than the family which raises none of its food. The same is true of families producing their milk, meat, or eggs. This is especially important in rural areas, especially mixed or general farming sections, where the farmers produce much of their own food. The value of food and fuel produced by consumers is not, however, included in many estimates of national income.

During the past decade, the money income of the American people has gone up faster than the prices of the goods and services which they purchase. This is a general statement. It does not, of course, apply to persons whose income is relatively fixed as those living on pensions, annuities, interest, and government employees such as teachers. Higher prices have meant hardship to many of these. On the other hand, the incomes of industrial workers, farmers, and businessmen have generally advanced faster than prices. This is due not only to higher wages and higher prices for the things they have to sell but to more regular employment, more workers per family, and overtime payments. This has meant a higher standard of living for the majority.

[4] Department of Commerce estimates of money income are incomplete as they do not include receipts from extra and odd job work by various members of the family, income from keeping lodgers and boarders in private families, and income from illegitimate and illegal pursuits. Other income that is omitted includes food and fuel produced by non-farmers, the services of the housewife, living costs of inmates of institutions, and living of salesmen and others while on expense accounts.

Total and per capita income. Total income was estimated at $80 billions in 1929, $71 billions in 1939, $92 billions in 1941, and $177 billions in 1947. Per capita income was $140 in 1859, $205 in 1899, $326 in 1913, $654 in 1929, $356 in 1933, $540 in 1939, $694 in 1941, and approximately $1,250 in 1947.

Taking 1926 as 100 the average per capita purchasing power was $482 in 1899, $589 in 1913, $681 in 1929, $495 in 1933, $663 in 1939, and $1,145 in 1944. These figures indicate an increased purchasing power of 35 per cent from the beginning of the century to 1939. There was a marked increase during the War years but in the adjustment period following the close of the War, prices tended to catch up with income although real income as measured in purchasing power was higher than in 1939.

Our standard or scale of living as measured by the use of automobiles, paved highways, radios, heated homes, modern plumbing, cosmetics, jewelry, magazines, books, newspapers, movies, and athletic events has increased. If we use the productive facilities developed during World War II, we will retain a standard of living at least 50 per cent above that of 1939. This is an important fact to the seller of goods and services. Whether this increased standard of living makes us any happier or improves our spiritual or mental life is another question and one beyond the scope of this book.

Distribution of income. Income is apparently more evenly distributed than at any time in our history. The following figures show estimates of the distribution of income and the number of families or individuals in each group:

INCOME LEVEL	PERCENTAGE DISTRIBUTION OF FAMILIES		
	1935–36*	1946**	1950***
Under $1,000	41	6	6
1,000–1,999	37	20	16
2,000–2,999	13	31	20
3,000–4,999	6	27	26
5,000–9,999	2	11	32
10,000 and over	1	5	

* National Resources Committee, *Consumer Incomes in the United States,* 1938.

** Daniel Starch, *Advertising and Selling,* March, 1947.

*** Dewhurst, J. Frederic, and Associates, *America's Needs and Resources.* These refer to consumer units and are estimated on the basis of continued prosperity.

Sellers are interested in the number of families and the total income received by the families or individuals in each group. Starch's estimate for 1946 follows:

INCOME LEVEL	PER CENT OF FAMILIES	NUMBER OF FAMILIES	AVERAGE FAMILY INCOME	TOTAL INCOME (BILLION $)
Under $1,000	6	2,400,000	$ 700	1
1,000–1,999	20	8,000,000	1,600	12.8
2,000–2,999	31	12,400,000	2,750	34.1
3,000–4,999	27	10,800,000	3,750	40.5
5,000–9,999	11	4,400,000	6,800	29.9
10,000 and over	5	2,000,000	23,000	46.0*
Total and average	100	40,000,000	4,100	165.0

* Income taxes take a large part of this amount.

A study of these figures is very helpful as families in different income groups spend their money in different ways—have different patterns of consumption. For example, low income families spend a larger proportion of their incomes for food while upper income families spend relatively more for amusement, entertainment, travel, and education. However, it must be remembered that income taxes must be paid before other expenses and that these take relatively more from the upper than the lower income families.

Regional differences. The foregoing figures are national averages. Average incomes vary widely between different parts of the United States. As a rule they are larger in the highly industrialized areas than in the agricultural areas. However, incomes vary widely between agricultural areas depending on the fertility of the soil and the type of farming.[5] Incomes are usually lowest in areas of poor soil, and in areas raising crops requiring much hand labor such as cotton and tobacco. They are uncertain in one-crop areas. They are usually higher in areas with fertile soil, or in areas raising dairy products, fruits, or vegetables. The United States Department of Commerce estimates the income of the various states for each year. There are also estimates of county incomes in some states and *Sales*

[5] For example, average per capita income varied from $179 to $1,212 in Illinois counties in 1939. Cf. Special Bulletin No. 4 of the Bureau of Economic and Business Research, Univ. of Ill.

Management magazine publishes annual estimates of consumer buying power in counties and trade areas. The businessman is especially interested in the income in the area in which he sells and the demand of the people in the area. The demands of the people in an area depend on their incomes, their industries and occupations, the climate, and their habits and customs.

Consumer Expenditures

In general we spend about 60 per cent of our income in retail stores, the exact percentages varying somewhat from one area to another. Food comes to mind first when we think of family expenses. The percentage of family income going for food decreases as the income increases. Food now takes about 20 per cent of our income, considerably more among low income families, and less among upper income families. Clothing takes about 10 per cent of our income; rent about 10 per cent; while fuel, electricity, furniture, home appliances, and other costs of home operation take between 10 and 20 per cent. Rent takes a higher proportion of family income in the north than in the south and more in large cities than in small towns and rural areas. Automobiles and other transportation take 8 per cent of our income. We spend about 4 per cent for medical care and drugs and another 4 per cent for reading matter, sports, and other forms of entertainment.

One estimate of total consumer expenditures is shown in the following table. It covers a fairly prosperous year when shortages of goods did not affect purchasing to any marked extent and when taxes were lower than at present. It may therefore be taken to represent our spending pattern in a fairly normal year. In this year we spent 60.5 per cent of our income for goods; 27.3 per cent for services; 4.4 per cent for direct personal taxes; and saved 7.8 per cent.

The amount left after a family pays for its food, housing, clothing, taxes, and medical care is called *discretionary buying power*. The discretionary buying power may be used in any way the family chooses—for an automobile, a new home, a fur coat, an electric refrigerator, for travel, education, jewelry, or

in other ways. The ways in which it can be spent are many and they change with fashions, fads, education, mass psychology, and the sales efforts of sellers. Since it is difficult to predict how this "loose money" will be spent, retailers, wholesalers, and manufacturers try to solve the serious problems in forecasting consumer demand for specific articles by constant study and research.

Table 4–1

EXPENDITURES OF AMERICAN CONSUMERS, 1941*

(000,000 omitted)

Goods	Dollars	Percentage of Income
Food	20,998	22.8
Tobacco	2,270	2.5
Alcoholic beverages	4,192	4.5
Clothing	9,500	10.3
Furniture, furnishings, appliances, radios, musical instruments	6,685	7.2
Household supplies	720	.8
Drugs, etc.	1,180	1.3
Toilet goods	570	.6
Books, magazines, stationery	1,450	1.6
Jewelry, including clocks and watches	710	.8
Autos, auto fuel, tires, accessories, pleasure boats	5,020	5.4
Fuel (coal and gas)	1,700	1.8
Toys, games, sporting goods	620	.7
Other goods	145	.2
Total for goods	55,760	60.5
Services:		
Housing	8,574	9.3
Home maintenance	1,548	1.7
Household utilities	2,444	2.6
Total housing	12,566	13.6
Personal care	1,772	1.9
Transportation	2,589	2.8
Medical care (inc. funeral expenses)	3,014	3.3
Recreation	1,948	2.1
Other	3,319	3.6
Total for services	25,208	27.3
Total consumer expenditures	80,968	87.8
Direct personal taxes	4,000	4.4
Savings	7,232	7.8
	92,300	100.0

* United States Department of Commerce, Bureau of Foreign and Domestic Commerce, study conducted by William H. Shaw.

Inclination to buy. Consumer inclination to buy is influenced by custom, habit, fashion, imitation, education, advertising, and salesmanship. Demand varies with race, climate, income, education, occupation, and religion. Some families spend much on clothing and live in a rented house. Some own attractive homes and spend little on travel. Others spend more on food, drink, and recreation. Some prefer leisure to work that would give higher incomes. The seller's task is to arouse the consumer's desire for his products. This he strives to do by advertising, salesmanship, publicity, propaganda, and window and store displays. The individual seller often can do little or nothing to change fashions or customs or to prevent them from changing. His job is to study trends, attempt to forecast correctly, and prepare for the changed demands.

The pattern of consumption. After tracing changes in consumption for thirty years, the Twentieth Century Fund[6] projects this pattern into the future to 1960. The percentage distribution of family expenditures, after taxes, follows:

	1940	1950	1960
Total	100	100	100
Food, liquor and tobacco	31.0	31.1	30.6
Clothing, accessories, personal care	13.9	14.0	13.9
Housing and utilities	17.8	16.6	15.9
Household equipment and operation	12.4	13.0	13.0
Consumer transportation	10.4	10.9	12.2
Medical care, insurance and death expenses	6.7	6.6	6.5
Recreation	4.6	4.9	5.1
Private education	1.6	1.5	1.5
Religion and private social welfare	1.6	1.4	1.3

Consumer Problems

The problems of the consumer may be grouped according to what, when, where and how much to buy, although the consumer does not customarily think of them in this manner. He usually thinks in terms of how to solve his problems rather than of what they are. The difficulty of his problems is accentuated by his general lack of marketing knowledge.

What to buy. The consumer buys convenience goods, shop-

[6] Dewhurst, J. Frederic and Associates, *America's Needs and Resources.* These percentages differ from those given in Table 4–1 because they apply after the payment of income taxes.

ping goods, and services. The consumer desires to buy convenience goods with a minimum expenditure of time and effort. Their unit value is usually low and they are fairly uniform in quality.

Since shopping goods are usually of relatively high unit value and both their quality and price extend over a wide range, the consumer is more deliberate in the buying process than when he buys convenience goods. Sometimes his deliberations may extend over a period of months during which he visits different stores and compares qualities and prices. He will spend considerable time and effort in buying these goods. Information may be sought from users, friends, and from printed sources.

The services which the consumer buys cover a wide range both in nature and price—from a minor repair on an automobile to the services of a highly skilled surgeon. Some services, such as those of a barber, shoe repairman, or of a cleaning and pressing establishment, are bought at the most convenient or nearest place and very little deliberation is involved. Like convenience goods, they are of low unit cost. Other services are purchased only after relatively long deliberation. Like shopping goods, the quality and price range is wide. Examples are courses of training for professional skills, architectural service, the use of a house or an apartment, and life insurance.

What the consumer buys also has been classified into durable and non-durable goods. Durable goods include such shopping goods as automobiles, electrical appliances, and furniture. Non-durable goods may be either convenience goods or shopping goods. This classification places emphasis on the rate of consumption and the frequency of purchase.

In determining what to buy the consumer attempts to get the best quality for the lowest price. As a judge of quality the consumer is frequently a rank amateur because he seldom has the opportunity, the facilities, or the knowledge to enable him to determine quality accurately. What knowledge he does possess is of those items which he purchases most frequently, that is, convenience goods. He may attempt to obtain more knowledge of merchandise with a high unit value but he is often unable to judge the significance of the information after he obtains it.

Who buys. It is often stated that the wife does the majority of the buying for the family. This is an overstatement. One survey shows that the woman of the family buys more than 90 per cent of her clothing, toilet articles, and kitchenware and draperies. She buys more than one half of clothing for the children, floor coverings and drugs. The husband buys most of his own clothing, hardware, fuel, automobiles and gasoline. Husband and wife frequently shop together for furniture, automobiles, rugs, and home appliances. Many purchases are made after family discussions. Although the wife may buy more than one half of the goods used by the family she buys many of them with the needs and preferences of the family in mind and some on instructions from other members of the family. The seller should realize that he must influence other members of the family in order to sell his wares, even though the purchase is made by the wife.

The consumer's decision on what to buy is influenced by advertising, salesmen, the movies, schools, magazines, radios, newspapers, friends and acquaintances. The influence frequently occurs at a time when the consumer is not thinking of making an immediate purchase.

Buying motives. The consumer's buying motives influence his decisions on what to buy, when to buy, where to buy, and how much to buy. Consumers buy because of certain fundamental drives or motives. There is no general agreement among psychologists as to what these motives are. Most consumers are aware that economy, pride, and comfort motivate many of their purchases. The consumer would also recognize, in a long list of so-called basic urges, that some of them also motivated his purchasing. Here is a representative list of these motives:

Desire for bodily comfort. Desire for food, health, protection from the elements (as given by houses and clothing), leisure, and cleanliness.

Affection. Love of the opposite sex, of family, of friends; and the desire to make them happy.

Pride. Desire for the praise and admiration of others, desire to excel, desire for ornaments, education, and so on.

Profit or desire for gain or economy. Most purchases made by businessmen are made in the hope of a profit.

Fear. Caution, desire for safety.

Imitation. Desire to be like others and have what they have; to be in fashion.

Worship, love, and awe of the Divine.

Constructiveness, desire to make things.

Curiosity. Desire for knowledge, education, travel.

Desire for justice and fair play.

Amusement. Desire for entertainment and recreation.

Acquisitiveness. Desire to own things.

How much to buy. How much to buy is frequently determined with exactness by the consumer in advance of purchasing and he buys accordingly. In many cases, however, the amount he buys is not predetermined. The present and possible future price is often an important factor in determining the quantity bought, but price is by no means the only factor. Due to inertia and habit the consumer frequently buys items in small quantities although he consumes a large amount over a period of time. He might buy such items in larger quantities and possibly have the advantage of a lower price and avoid the inconvenience of frequent purchasing. The consumer's income may be a limiting factor, however. The hope or the possibility that the price will be lower in the future may also be a limiting factor.

The perishability of certain food products affects the quantity purchased. The lack of storage space and facilities in many homes often makes it impractical to buy in larger quantities, although the construction of community food lockers and improvements in home refrigeration have somewhat overcome this limitation.

An important factor in determining the quantity purchased is the fear that the supply of some desired product will be scarce in the future. Although the consumer realizes how heavy buying will affect the price, his desire not to be inconvenienced by any shortage is equally if not more important. The scarcities which develop during war periods have made the

consumer very sensitive to the possibility of merchandise shortages and the attendant inconvenience.

When to buy. When to buy is a problem which ranges from determining on what day and at what hour to buy groceries to determining in what year to buy an automobile or a house. The consumer, in arriving at a solution of the problem, attempts to analyze market conditions. He intends to buy when prices are lowest and assortments are largest. The selection of this ideal time is difficult, however, because he is often uncertain as to when suitable conditions exist.

Some convenience merchandise is bought with a very small amount of deliberation; that is, on impulse.

Where to buy. Where to buy is a problem faced by every purchaser. As with the other buying problems, the amount of deliberation varies according to the purchase. Convenience goods are available in many places and it is often a matter of little consequence to the consumer where he buys. When the purchase is of some importance the consumer gives more consideration as to where he buys it. Among the factors he considers are price, the reputation of the store, the pleasantness of the contact with the salespeople, and the services extended by the store. The consumer's prejudices and habits also influence his decision.

The Consumer and the Store

The consumer's most significant contact with the store is made through his relations with the salespeople or other employees. To the consumer, the salespeople are the store. When he has pleasant relations with one or more salespeople in a store, he speaks favorably of the store. When his contact with a salesman is unpleasant, he expresses a dislike for the entire store. It makes but little difference whether the salesman is an untrained part-time employee or a full-time employee whose connections with the store are soon severed; if the consumer's contacts in the store are unpleasant a poor impression is made which may be lasting.

It is true that customers themselves are not always civil in their contacts with salesmen. It is difficult, however, for a store to justify discourteous treatment of such uncivil customers. Unpleasant customers are of no personal consequence to the salesman. His object is to handle all customers skillfully so as to sell them merchandise.

Sales and advertising service. The customer desires that the salespeople be prompt, informed, and courteous, and it is quite possible to reach a high degree of efficiency in these respects. It can be done by having a good class of salesmen and saleswomen. Superior salespeople command a higher income which may have to be reflected in higher prices. Some consumers, however, are willing to pay a higher price for the merchandise in order to secure this type of selling service.

The advertising service of a store is seen or heard by many consumers, a portion of whom may be or may become customers of the store. Generally the consumer notes the scarcity of adequate information in retail advertising and the lavish use of vague superlatives. He is skeptical. He believes much advertising to be deceptive. To the extent that the advertising is not believed or does not provide satisfactory information, the advertising is inefficient.

Credit service. Credit is a service desired by a large number of customers. Obviously the performance of this service involves some expense. Although no separate charge is ordinarily made when merchandise is bought on open-book accounts, the store cannot perform this service without cost. The credit operating cost is included in the general expenses of the store and is covered by the markup on the merchandise. In a credit store, both cash and credit buyers pay for the extension of credit. Even so the price of the merchandise may be lower (due to other factors) than it is in stores which do not extend credit.

Many customers, either willfully or because of the seller's failure to explain, do not understand their obligation when they buy merchandise on account. They may have only a vague notion that they must pay for the merchandise within a given period. The retailer, in his eagerness to increase his sales volume, encourages buying on credit. The customer because of

weakness sometimes buys more than he can pay for in the usual credit period. When the store finds it necessary to take vigorous steps to collect the account, such customers, of course, do not understand.

Many difficulties can be avoided for the store and for customers if the seller will carefully explain credit services to his customers. He should not assume that the customer understands his obligations when he opens an account. A letter, brochure, or at least a verbal explanation of the service should be given to each customer.

Least understood by consumers is the service of installment credit. Only a small percentage realize how much it costs. Some who know what it costs cannot overcome their desire to have the merchandise "now." The cost of the service seems small when spread over a period of months.

Retailers have been criticized for selling merchandise on installment. Consumers, however, have been willing to buy on this basis, otherwise this credit extension method would not have developed. The criticism is that the method encourages the consumer to buy more than he can afford, but the same might be said of buying on terms such as payment within thirty, sixty, or ninety days. Although the extension of credit has at times encouraged over-buying, the bad judgment of the consumer is to be criticized just as much as that of the retailer who encourages a greater use of credit than conditions warrant.

Delivery service. Delivery service is convenient for the customer and it holds and builds business for the retailer. In asking for this service, however, the customer has often gone to extremes—for instance, asking for delivery of a quarter of a pound of butter. The retailer just as foolishly has provided such extremes of service. During World War II a semblance of sanity was established in the extension of this service, but competition will not permit wartime standards of delivery service to prevail in peacetime. For bulky items the store probably can provide delivery service more conveniently and economically than can the customer. Small articles can just as well be carried by the customer and will be if the customer is asked to do so. Even some large articles can be transported in

the customer's automobile but too often he is not asked to do so.

Delivery service involves additional operating expense. Trucks, drivers, and supervision of the service are all required. The service can be paid for by charging those customers who request it but this practice is usually unpopular with the customer. Consequently, as with the credit service, the operating cost is included among the expenses of the firm and covered by the merchandise markup.

Returning merchandise. The privilege of returning merchandise is a service which some stores have permitted customers to abuse. The customer expects to easily return anything which he doesn't like. Some customers "buy" merchandise with the intention of returning it. Stories are told of customers who obtained dresses and house furnishings for a party with the intention of returning the merchandise the next day. Such extreme cases indicate how far certain customers will go in abusing the return privilege. Consumers give little or no thought to the cost of such service and retailers have devised no practical method of charging for it. Store expenses on returned merchandise include the costs of returning the goods to stock, crediting the customers on the books; and often the transportation cost in bringing the goods back to the store. Furthermore, if the merchandise is soiled or otherwise damaged, it must be marked down to sell it.

A few stores refuse to permit merchandise to be returned, but competition will not permit widespread adoption of such a policy. A customer who is refused the privilege of returning merchandise may cease to be a customer. What is more important, he may discuss the incident at every opportunity and make a special effort to place the store in an unfavorable position.

Merchandise information. For those consumers who desire to obtain more information about the merchandise, the retailer can buy products that have informative labels and instruction booklets. Sales clerks in stores can also be supplied with more product information. The customer has more confidence in the store, the salesclerk, and the merchandise when he is provided with product information rather than vague generalities. Too frequently, the customer is not instructed properly in the care

and use of merchandise. When unsatisfactory service is obtained from the merchandise the customer rightly or wrongly holds the store responsible.

As has been previously indicated, some of the larger retailers have recognized the consumer's desire for grade labels and have provided them. The small retailer may not be in a position to do this directly but he can use his influence to induce manufacturers to be more aware of consumer desires. Grade labels, although not practical for every product, should be used in those instances where consumers show a strong desire for them.

Other services. A number of other services which retailers perform for customers are also based on customer contacts. Among them are parking service, check cashing, children's playrooms, and gift wrapping. Perhaps the customer would not object seriously if some of these services were withdrawn, but it is a debatable question as to which ones, if any, should be discontinued. Experimentation may provide a satisfactory answer. All services involve some risk to the store.

Perhaps the greatest service extended to consumers is offering the right merchandise at the right price. This means selecting in the wholesale markets the merchandise which the consumers in the community desire. It means that quality, service, and price must be in the proper relationship in order to make a lasting impression on the consumer. Since the majority of stores depend on repeat business from the same customers, the reputation which they build for price, service, and quality is fundamental.

Questions

1. What effect has the tendency toward urbanization had on markets?
2. What is the significance of the following factors from a marketing point of view?
   (*a*) Birth and death rates
   (*b*) Tendency to marry earlier
   (*c*) Tendency of the population to age
   (*d*) Tendency of the size of the family to decrease.
   (*e*) Tendency of married women to constitute a greater proportion of those gainfully occupied

3. What is the weakness of per capita income as a standard-of-living indicator?
4. What percentage of families had a real income of less than $3,000 in 1946? A money income of less than $3,000?
5. What is discretionary buying power?
6. What are buying motives?
7. How do buying motives influence what, when, where, and how much to buy?
8. What does the customer expect from a store in the way of selling service? Advertising service? Credit service? Delivery service?
9. Should customers be permitted to return merchandise whenever they please and for any reason? If not, what limitations should be placed on this privilege?
10. How can the percentage of returned goods be reduced?
11. How may the customer be provided with more product information?
12. Why do some stores perform a number of miscellaneous services for customers?

II. *Wholesale Marketing*

A. Organizations

5

Commission Merchants, Brokers, and Auctions

MIDDLEMEN who buy and sell for others are called agents and those who employ the agents are called principals. The buying and selling of goods on a commission basis is a method by which the owner or prospective owner directs some one to sell or buy goods for him. A fee or percentage of the value of the goods bought or sold is paid for performing these services. There are several different kinds of agents, consequently the nature of the agent-principal relationship varies.

Commission Merchants or Factors

A commission merchant or factor is an agent who for a compensation called commission (or factorage) sells goods consigned or entrusted to his possession by or for the owner. The terms factor and commission merchant are synonymous and no important court decision on the point has held to the contrary.[1]

A commission firm may conduct more than one kind of business. Some may buy and sell on their own accounts and also handle goods on an agency basis. They may at times employ

[1] The term factor was common in the South. English merchants in colonial times called their agents in this country "factors." The later development of the cotton trade and the early importance of the English in that trade caused the usage to persist. In the North, the early traders were called "merchants" and usually did not owe their start in business to an agency relation with an English firm. They bought and sold on their own account but would often buy the products of this country for foreign firms on a commission basis, and likewise sell foreign goods here on commission. The words commission and merchant were thus in common use and they were retained to describe those later middlemen whose chief business was on a commission basis.

auctioneers and hold auctions, act as brokers, operate cold storage and other types of warehouses, and conduct any other kind of special business which might be profitably performed in connection with their general functions as a commission firm.

To be a commission merchant, one must have possession of goods, be engaged in the business of selling such goods for others, and be understood to receive a compensation for service rendered. If the merchant holds invoices and bills of lading for goods which have been entrusted to him to sell, he is said to have constructive possession. The agency contract may be written or oral, or it may be implied in the actions of the principal and factor. The instructions of the principal to his factor should be clearly stated because the factor is bound to follow them even though his best judgment tells him to act otherwise. If instructions are not given, it is understood that the usages and customs of the particular market will be followed.

Commission merchants are important in the sale of livestock, grain, fruits and vegetables, dry goods, cotton, naval stores, poultry and poultry products.

Table 5-1

BUSINESS OF COMMISSION MERCHANTS, BROKERS AND AUCTION COMPANIES IN 1939

(Census Figures)

TYPE OF AGENT	NUMBER	NET SALES (Millions)	EXPENSES (Per cent of sales)
Total	20,903	$11,201	2.7
Brokers (free lance)	4,710	3,391	1.5
Manufacturers' agents, without stock	7,871	1,145	4.0
Manufacturers' agents, with stock	1,907	252	11.7
Selling or sales agents	1,487	1,742	3.7
Commission merchants or factors	2,758	2,748	2.5
Import agents	394	343	2.0
Export agents	654	571	2.9
Auctions	649	434	3.2
Others	473	575	1.8

Services performed. The most important service of commission merchants or factors is selling. They are usually located in central markets where they are in constant touch with sup-

ply, demand, and price activity. They are good judges of quality. They know who are buyers. The commission merchant often pays the freight and drayage on the goods, has them insured, and sometimes has them regraded or repacked. The cost of these services, plus his commission, are deducted from the receipts before remitting the balance to the owner of the goods. The factor often supplies his principals with information on prevailing prices.

The owner of the goods may set the price at which the goods are to be resold; if no instruction is given, the factor must sell at the best current price. Manufacturers, in order to control the prices at which their goods are resold, sometimes consign goods to wholesalers or retailers, who thereby become factors. This was a fairly common practice prior to the passage of laws, the so-called "fair" trade laws, permitting the control of sale prices by contracts.

The factor is prohibited from making a sale to himself or to a partnership of which he is a member unless his principal (the owner of the goods) with full knowledge of the facts consents to the sale. The factor may be authorized to sell on credit and when this is the case he must use reasonable care in determining the credit standing of the buyers. He may also collect the accounts for his principal. Usually when credit sales are made the factor assumes the risk of nonpayment. Such agents are known as *del credere* factors.

The commission merchant has for many years financed or helped finance his principals. In the fruit and vegetable, and cotton trades he often advances money to the farmer before the crop is harvested. Factors were for years important in the cotton trade but their business declined as other agencies took over the financing of the growers. The commission houses often render valuable financial assistance to the textile mills by discounting their accounts receivable, endorsing their notes, or loaning them money. The procedure of discounting their notes has come to be known as "factoring."

Factoring. In factoring accounts, the factor examines the credit standing of the customer before the sale is made, advances money when he receives copies of the invoice and bill of

lading, and then either collects the account himself or has the mill collect the account for him. The factor thus becomes a credit and collection department for the mill and also acts as a banker. Many of the firms engaged in discounting accounts receivable have ceased to perform selling or other functions for the mills. Factoring, however, is adapted only to trades with fairly long credit periods. It is impractical to factor accounts that are payable in ten or twenty days. For this reason factoring is unsuited to the food trades. Factoring usually is not available to manufacturers or wholesalers selling to small retailers because the former's sales are too small for profitable handling. Businessmen who sell in reasonably large amounts on fairly long credit should investigate the possibility of factoring their receivables if they need additional working capital.

Criticism of commission merchants. Commission merchants have been adversely criticized for selling goods to themselves, for not obtaining the best prices, and for making fraudulent returns to shippers. The commission merchant has the goods in his possession and as an agent is duty bound to sell them to the best advantage and make an honest accounting to the owners. Because he often operates at a distance from his principals and may never see some of them, they may be unable to supervise his operations or check on his efficiency as a salesman. He has the opportunity to slight their interests and to defraud them by making dishonest returns. Some have been dishonest; others have done their best and made honest returns but have been suspected of dishonesty. Partly for these reasons, the commission business in certain trades has been declining in relative importance for many years. In spite of these criticisms, however, the commission merchant is still important in several trades, especially livestock and grains.

Brokers

Definition. A broker is an agent who for a fee or commission called "brokerage" negotiates sales or purchases of goods or other property which he does not have in his possession. He differs from the commission merchant or factor in two respects:

he is not entrusted with possession of the property, and he is not authorized to sell or buy in his own name. The broker thus has less authority and is more restricted in his activities than is the factor. He is an independent businessman and not the employee of a principal.

There are three types of brokers who sell merchandise: free-lance brokers, manufacturers' agents, and selling or sales agents. The free-lance or pure broker is not bound permanently to any set of principals but sells anywhere and at any time that he finds an opportunity. The manufacturers' agent is bound to his principals for definite periods, represents them in specified and limited territories, and sells at prices designated by them. He represents a limited number of principals and sells only a part of the output of each. He may or may not carry stock. Those who carry stock are legally commission merchants operating under definite instructions, but they are commonly referred to as "manufacturers' agents." The sales or selling agent usually sells the entire output of his principals, with whom he maintains continuous relations, and often acts as the sales department of the companies he represents.

The broker has delegated authority, either expressed or implied, necessary to carry out his duties. His acts are binding on his principal unless the broker exceeds his authority. The broker may be given authority to guarantee the goods, but otherwise he cannot make such commitments. Ordinarily he does not have authority to pass title; when he does pass title, he is usually acting as a factor.

The broker usually earns his commission as soon as the contract is completed and legally can collect the fee whether or not the sale is ever consummated.

The broker may be limited to contracts at prices specified by his principals; may secure offers which he submits to his principals for acceptance or rejection; may make sales "subject to approval of prices" by his principal; or may use his own discretion in accepting prices and entering binding contracts. The manufacturers' agent usually sells at the prices specified by his principals, or makes sales subject to approval of prices by them. The free-lance broker usually submits offers for acceptance or

rejection, or sells at specified prices. The sales agent often has authority to agree on prices and complete the contracts without referring them to his principal for approval.

Brokers usually sell in large quantities and operate at low costs. Commission rates vary from one fourth of 1 per cent to 5 per cent; rates of 2 or 3 per cent are common.

Services performed by brokers. The two main services or functions rendered by brokers are selling and giving advice. The broker finds buyers (or sellers, in case he is a buying broker), negotiates the price, and sometimes closes the contract. Brokers are usually in central markets and operate in highly specialized fields. They may sell cotton cloth, canned foods, chemicals, coal, or sugar. They know the buyers and sellers. They are in constant touch with the movement of prices. They have their fingers on the pulse of supply and demand. They sense trends in prices. Consequently many business concerns use brokers for information on prevailing prices and price trends, for advice on whether to sell or hold goods for higher prices, or (if buying) whether to stock up or buy from hand-to-mouth and wait for prices to decline. Some brokers sell their price information as a service. Since free-lance brokers want to make immediate sales they are less likely to advise waiting for price changes than are selling agents.

Brokers do not, as a rule, finance their principals although some, particularly the sales agent, help finance the plants they represent. They may collect accounts and represent their principals in arbitrating disputes. Brokers ordinarily do not actively promote sales unless they receive an additional fee. Manufacturers' agents and selling agents do some sales promotion and have placed many new brands on the market.

Criticism of brokers. The adverse criticisms of brokers are that they do not actively promote the sales of the principal's goods, that they do not secure the best prices, that they tend to lower prices, and that they do not represent the interests of their principals in the settlement of disputes. It has been said that brokers are more interested in earning commissions than in holding out for the best prices and that they often advise their principals to sell at slightly below the market prices in

order to make sales and earn commissions. In short, it is alleged that brokers are poor salesmen who do not fully represent the interests of their principals.

On the other side, it is pointed out that brokers usually work for relatively small rates of commission and that for 1, 2 or 3 per cent the seller cannot expect much sales promotion. Brokers say that they have placed many new products on the market only to have them taken away once they have established the market. In their opinion, this proves that they do actively promote sales. On the other hand, the manufacturer often takes his product from brokers and places his own salesmen in the field even though he knows the new program will increase his selling expense. Brokers maintain that they will use salesmen to promote a manufacturer's product if the special service is paid for.

Conclusion on brokers. Brokers are especially adapted to the need of small manufacturers with small organizations or limited knowledge of marketing and selling. Small businesses, especially newcomers, are often unable to afford large sales departments; their capital is usually limited. Their products are often unknown to the consumers and have to be sold on the basis of quality and price. Such manufacturers often turn their selling over to selling agents who market the entire output and who may help also to finance operations. When the firm grows and its members learn more about marketing, they may use manufacturers' agents. Eventually they may establish their own sales organization. A sales department may increase the percentage cost of selling but the increased sales should warrant the higher cost.

The broker supplies an inexpensive method of selling. His services are suited to the needs of the maker of staple goods sold on a price basis. Such goods are usually sold at the prevailing prices and a good broker handles transactions satisfactorily, thus relieving those manufacturers who prefer to devote their entire attention to production. Some believe it wise to devote complete attention to efficient plant operation. If the plan succeeds, they may have very profitable businesses.

Purchasing agents. Purchasing agents, or buying brokers, are

independent businessmen; they should not be confused with salaried executives of manufacturing plants and institutions who are often called "purchasing agents." The buying broker is paid a commission by those who employ his services. Such brokers are important in the hardware, building materials, produce, and several other trades. The hardware wholesaler handles so many thousands of items made by so many hundreds of producers that it is difficult for him to maintain direct contact. He therefore employs purchasing agents to find and buy the desired goods, to combine orders to secure lower prices, and to give information. The latter is particularly valuable. The purchasing agent thus performs much the same services for the buyers as do other brokers for the sellers.

Resident buyers. This term is used largely in the women's apparel and dry goods trades. Fashion is so important in these lines that goods must move quickly from producers to retail stores. For this reason, the dry goods wholesaler has been nearly eliminated except in the sale of staple goods and lower priced garments sold to small retailers. The wholesaler has been replaced by the resident buyer who is employed by the retailer to keep in contact with sellers, to follow fashions, to direct the store's buyers to good sources of goods when in the market, and to buy for the store when goods are needed between visits of the store's buyers. Most resident buyers are located in New York City, although some are found in other cities. Certain large department stores maintain permanent buying offices in New York while others employ resident buyers.

Auctions

Definition. An auctioneer is an agent who conducts a public sale where purchasers make bids, by sign or outcry, for commodities or property; the bidder who makes the highest and best bid usually obtains the property.

The auctioneer differs from the broker in that he usually has possession of the property. In this respect he resembles the factor, but the auctioneer differs from both broker and factor in that auction sales are public sales whereas sales made by a

broker or factor are private negotiations. Private sales by auctioneers are, as a rule, not allowed. Some auctions are conducted by companies that also do a commission or brokerage business.

Method of operation. The owner of commodities offered for sale at auction has the right to control the sale until it is legally made. He may prescribe the manner, conditions, and terms of sale on a poster or in a catalogue, or have the auctioneer proclaim them. It is important to note that the conditions of an auction sale, announced by the auctioneer at the time and place of the sale, are binding on the purchaser whether or not he knew, heard, or understood them. Buyers at auction should remember the old rule, *caveat emptor* (let the buyer beware), because goods are usually sold "as is" and not warranted. The buyer is supposed to inspect them carefully before bidding. Bids may be made orally, in writing, by pressing a button, by nodding the head, or by some sign which only the auctioneer can see.

Auction companies provide places where the goods are displayed for inspection and frequently supply catalogs listing the goods offered for sale. Auctioneers provide clerks to record sales, and in general make prompt payment to the owners of the goods. Sometimes credit is extended to the buyers for short periods. Auction companies are usually paid a commission on sales plus handling charges for unloading the goods, arranging them in the display or auction room, and for removing them from the floor or making deliveries to the buyers.

Sales often proceed rapidly. The tobacco auctioneer makes several hundred sales per hour and the fruit auctioneer goes almost as rapidly. Because one auctioneer can sell a large volume of goods in a day the auction is an economical method of selling. Auction buying, however, is often expensive. For each auctioneer there are usually several buyers whose time is valuable. Unless a buyer makes many purchases he may find that his expenses are too high.

An auction puffer or by-bidder may be employed by the owner of the goods to raise the price by fictitious bidding. A sale in which a puffer is used is void, or voidable at the pur-

chaser's option. In order to hold the price down, buyers sometimes agree not to bid against each other. This procedure voids a sale to one who is a party to the agreement. Auctioneers sometimes "pull bids out of the air," that is, they announce fictitious bids. The existence of such abuses has probably caused auction selling to decline in some trades and limited its growth in others.

Importance of auctions. The Census reported 649 auction companies with sales of $434,000,000 and average expenses of 3.2 per cent of sales for 1939. The most important goods sold at auction are leaf tobacco, fresh fruits, furs, livestock, naval stores (turpentine and rosin), sponges, works of art, and used furniture and farm equipment. Practically all leaf tobacco, except cigar types, is sold at auction. The bulk of citrus fruits reaching our large eastern and middle western cities is sold at auction, as are many of the furs used by manufacturers in New York and St. Louis.

Auction sales may be divided into four classes. First, those which concentrate raw materials and pass them on to processers. The commodities sold include tobacco, naval stores, sponges, livestock, eggs, wool (domestic and foreign), fruit, and furs. Second, auctions in central markets which divide goods and sell to wholesalers, jobbers, and large retailers. The fruit auctions come in this class. Country auctions, including some livestock sales, and so-called "retail" auctions which sell used furniture, farm equipment, and other goods direct to the users are a third class. Auctions of antiques, art goods, and "collectors' items" constitute a fourth class.

Criticism of auction selling. Auctions are a quick and inexpensive method of selling but often a relatively expensive method of buying. They furnish an outlet for goods of uncertain value such as real estate, ungraded goods, or goods with no established market. They are open to the public and anyone can bid. Trustees, receivers, and sheriffs, who use the method frequently, usually specify "public sale" to prevent the trustee from selling goods privately at less than their real worth to friends or accomplices.

Auctions are said to supply open markets and to give free

play to supply and demand. Since supply and demand vary, however, auction prices often fluctuate widely. Judgments as to quality and adequacy of supply are often made quickly with the result that a variety of prices is paid for similar goods in a single day. Uncertainty as to prices that will prevail limits the quantity of goods offered at auction. When well patronized, auctions provide a very efficient marketing method. Their use would probably be more widespread except for the abuses mentioned on pages 83-84.

Questions

1. What is a factor?
2. What services are performed by factors?
3. Can a factor make a sale to himself?
4. What is a *del credere* factor? *Caveat emptor*?
5. What is meant by the term "factoring"?
6. What criticisms have been made of factors?
7. What is a broker? How does he differ from a factor?
8. What are the three types of brokers?
9. What services are performed by brokers?
10. What criticisms have been made of brokers?
11. What is a purchasing agent? A resident buyer?
12. What is an auctioneer? How does he differ from a broker and a factor?
13. How does an auctioneer operate?
14. What are four classes of auction sales?
15. What criticisms have been made of auction selling?
16. Why is it that manufacturers often employ sales agents when they are small and then discharge these agents and establish their own sales organizations when they become large?
17. It has been said that the brokers cannot create demand—that they are best suited for selling staple products to large buyers on a price basis. On their side, the brokers say that they can create a demand if they are paid for doing it. They point out that little promotion work can be done for one, two, or even five per cent. If the manufacturer advertises his product and employs sales representatives, his expenses will be much above five per cent.

    The broker also says that if he expends a lot of energy on a brand and builds up a big demand for it, the manufacturer may take its sale away from him and not allow him to profit from his efforts.

Comment on these statements. Under what conditions would you employ a broker to create demand for goods sold under your brand?

18. Can a manufacturer sell more cheaply through his own salesmen or through a broker? Discuss.
19. If brokers sell at less expense than manufacturers' salesmen, should their operations be encouraged?
20. Sellers naturally have their goods sold in the way that they think will bring them the highest prices. Those who use the auction believe that they receive higher prices at auction than they would at private sale. Do you agree? Why or why not?

6

The Wholesale Merchant

WHOLESALERS are composed of two main classes. One class takes title to merchandise while the other does not. The former are known as merchant wholesalers or wholesale merchants. Those who do not take title to merchandise but act as agents for others are known as agent or functional wholesalers.

The agent wholesaler (discussed in Chapter 4) acts for another person or organization called a principal and performs certain specified services for which he is paid a fee or commission. The wholesale merchant hopes to make a profit by selling merchandise for more than he paid for it. He often performs the same services as an agent wholesaler but since no one has agreed to pay for his services, the wholesale merchant takes a chance that he will earn a profit. The term "jobber" is generally used as a synonym for wholesale merchant.

Types of Wholesale Merchants

Service or full-function wholesale merchants buy and carry goods in stock, have outside salesmen to solicit business, extend credit to their customers, and frequently deliver free to nearby retailers. Service wholesalers are the most important type of wholesale merchants. There are more of them and they have larger sales than any other type. They buy in relatively large quantities, and stock the goods in warehouses from which they can be delivered quickly to retailers and industrial buyers. They divide the large lots into smaller lots and repack them

when necessary for shipment to their customers. Goods may be delivered direct or turned over to railroad or trucking companies. They usually extend credit to the retailers, which necessitates keeping books and making collections, and often advise the retailer on how to operate his store profitably. The larger wholesalers operate chains of warehouses.

Drop shippers solicit orders from retailers, contractors, and industrial buyers, buy the merchandise, and supervise deliveries to buyers without handling the merchandise itself. They do business from offices and do not operate warehouses. They are important in the sale of coal and building materials. In the sale of these products, drop shippers compete with brokers and commission merchants. All operate in much the same way, except that drop shippers own the goods, take the risks of ownership, and operate for profit rather than a commission.

Table 6–1

WHOLESALE MERCHANTS, 1939

(Census Figures)

TYPE OF WHOLESALE MERCHANT	NUMBER OF ESTABLISHMENTS	AVERAGE % EXPENSE	SALES
Service or full-function	91,323	13.6	$18,688,897,000
Cash-carry	1,198	5.5	108,902,000
Drop shipper	937	6.4	474,891,000
Truck jobber	2,398	12.2	30,259,000
Converter	631	9.7	425,167,000
Exporter	586	7.7	778,001,000
Importer	2,158	8.3	1,379,575,000
Industrial distributors	1,471	16.7	729,650,000
Voluntary group wholesalers	703	11.4	108,902,000
Retailer co-operative warehouses	222	6.3	222,296,000

A drop shipment is a shipment of goods direct to the retailer or other buyer while the goods are billed to the wholesaler, who pays the manufacturer and collects from his customers. The legal sale is therefore made to the wholesaler but the producer ships the goods direct to the retail customers. Drop shipping saves the expense of handling the goods through the

wholesaler's warehouse. Sales are often made by the manufacturer's salesmen, in which case the wholesaler has only the expense of bookkeeping, carrying the account, and making the collection. Drop shipments are often handled by the wholesalers on narrow margins, perhaps 1 or 2 per cent. Some wholesalers have a large proportion of their goods drop-shipped in order to reduce operating expenses and selling prices.

Cash-carry wholesale merchants are limited-function wholesalers who do not sell on credit, use outside salesmen to solicit orders, nor make free deliveries. They have come into existence because they sell at lower prices than the service wholesalers and thus help retailers to meet the competition of chain stores. Ninety-five per cent of the business of cash-carry wholesalers consists of food (groceries, fruits and vegetables, and poultry), tobacco, and candy. They usually handle limited lines of merchandise composed largely of staples and other fast-moving lines. Since their warehouses must be close to the retailers many cash-carry wholesalers operate chains of small warehouses. To meet the competition of cash-carry wholesalers many service type grocery jobbers have added cash-carry departments.

The Census reported operating expenses of cash-carry grocery wholesalers to be 5.2 per cent. Compared with an average of 9.6 per cent for service wholesale grocers, some of whom operate cash-carry departments, this seems to indicate that the retailers can save almost 5 per cent by patronizing cash-carry houses. To do so they either must go after the goods, pay cash for them, and bring them to their stores; or they must phone or mail in their orders and pay the delivery charges.

Truck or wagon jobbers carry goods with them and sell and deliver on the same call. Some drive their own trucks while others have several trucks operated by driver-salesmen. They sell principally perishable or semiperishable foods (dairy products, fresh fruits and vegetables, meats); food specialties (salad dressing and potato chips are examples); confectionery; gasoline and oil; and tobacco. Truck jobbers are especially important in serving small retailers in neighborhood and in suburban areas. They may grant credit for short periods or sell for cash. Many truck jobbers operate from their homes and keep extra

stocks in their garages or basements. Truck jobbers probably do more business than is reported by the Census for the reason that the census enumerators may have missed many of them.

Truck jobbers usually have higher expenses than the orthodox type of service wholesalers. The chief service they render is regular delivery of perishables, semiperishables, and of specialties.

Converters buy unfinished cloth ("in the gray"), have it printed, dyed, or bleached, and sell the finished cloth to garment manufacturers, wholesalers, department stores, chain stores, and others who buy cloth in large lots. Converters select patterns and colors which they think will sell and contract for the various finishing jobs. They do not operate printing and dyeing plants but are specialized middlemen whose main function is fashion forecasting and taking risks which many mills do not want to assume.

Exporters sell to industrial consumers, wholesalers, and other large buyers in foreign countries. Importers sell to United States wholesalers and industrial users which they may contact through brokers. Exporters and importers differ from export and import *agents* in that the first group own the goods and are merchants.

Industrial distributors sell largely to industrial users such as manufacturers, contractors, mine and oil well operators, public utilities, and railroads. They are especially important in the sale of hardware, oil well supplies, plumbing goods, and heating equipment and supplies. Average operating expenses are given by the Census as 16.7 per cent, which is higher than for many types of wholesalers. This may be explained by the fact that they often carry very wide or diversified lines, that they fill many small orders for supplies or parts needed in making repairs, that they have outside salesmen, extend credit, and that many of them issue catalogs.

Voluntary group wholesalers are service or limited-function wholesalers who organize and sell to groups of independent retailers. Most voluntary group wholesalers sell groceries. Some handle hardware, variety goods, automobile accessories, and other lines. The retailers buy from them and in return receive

low prices, merchandising assistance, or help in advertising. The theory of a voluntary chain organized by the "voluntary group" wholesaler is that (1) retailers will buy all or most of their goods from the sponsoring wholesaler so that he can dispense with his salesmen; that (2) retailers will pay their bills promptly so that he will have less money tied up in accounts receivable (3) retailers will order in fairly large quantities. As a result, the wholesaler can reduce his expenses and his prices to the retailers. The wholesaler employs supervisors or salesmen-supervisors who give the retailers assistance in the selection and display of goods, and in solving advertising, accounting, or other merchandising problems. Voluntary wholesalers often provide advertising for their retail members. If there are several retailers in a town, they may place advertisements in the local papers and prorate the cost among the retailers.

When a retailer signs a contract, the voluntary wholesaler may send a man to rearrange the store, help the retailer select his stock, and instruct him how to operate the store in accordance with the policies of the group. Some wholesalers require the retailer to purchase the services of a supervisor for a given number of days each year, and to pay for accounting service when needed. Other wholesalers have very loosely organized groups, and do very little for the retailers except to furnish them with goods for week-end specials, or leaders, and to give advertising assistance. In the grocery trade most voluntary group wholesalers have higher average operating expenses than the service wholesalers, which would indicate that the former are unable to sell at lower prices than other wholesalers. In such cases the retailers' main membership advantage is the merchandising and advertising assistance received, and goods supplied as leaders. On the other hand, some voluntary wholesalers with low expenses, sell at low prices, and also give merchandising assistance.

Retailer-owned or co-operative wholesalers are wholesale houses owned and operated by groups of retailers. Retailers operate their own wholesale houses to reduce wholesaling expenses and to buy at lower prices. They own the stock and elect the manager. Retailer-owned houses usually carry limited

stocks of fast-moving lines, secure low-rent locations, and economize on officers' salaries and on equipment. In order to reduce expenses, they have no salesmen (unless a salesman is employed to secure new members), give a limited delivery service, and extend credit for short periods. A typical house makes one free delivery a week and extends credit for one week. In the grocery trade expenses of retailer-owned wholesaler groups and cash-carry wholesaler groups are the same. A retailer thus can buy as cheaply from a retailer-owned house as from a cash-carry house; at the same time, his goods are delivered, he receives a limited amount of credit, and very often is given assistance in advertising and merchandising. Many co-operative wholesalers arrange for the retailers to sponsor group advertisements. As a rule, they do not render as much merchandising assistance as do the voluntary group wholesalers. The retailers who operate their own wholesale houses usually go on the theory that the best way to meet chain competition is to buy goods cheaply enough to meet chain store prices.

Most retailer-owned wholesalers handle groceries but there are a number of such wholesalers selling drugs, hardware, and other lines.

Bulk tank stations are operated by oil refiners and independent wholesalers to supply filling stations, industrial users, and farmers with gasoline, oil, and fuel oil. The large tanks are filled from railroad cars, barges or boats (on waterways), or pipe lines. Tank trucks are used to deliver their goods. Most of the bulk tank stations are operated by oil refiners.

Assemblers of farm products are dealers who buy products from the farmers or country buyers and pass the products on to processors or to dealers in central markets. According to the 1939 Census about 30,000 assemblers were operating grain elevators, warehouses, cream stations, produce houses, or buying cotton, fruits, potatoes, livestock, and other products.

Integrated Wholesalers

Integrated wholesale houses are those operated by manufacturers or retailers (1) for the sale of their goods to retailers and

industrial buyers, or (2) for the purchase of goods from the manufacturers. The three important types of integrated wholesale houses are manufacturers' branch houses, manufacturers' branch sales offices, and chain store warehouses. The 1939 Census reports some 13,000 branch houses and some 5,000 branch sales offices. Bulk tank stations operated by oil refiners are manufacturers' branch houses. Retailer-owned wholesale houses might be considered as integrated wholesalers although owned by a group of retailers rather than by one retailer.

Manufacturers' branch houses carry stocks of goods and employ salesmen to sell to retailers and industrial buyers. Manufacturers' branch sales offices operate in much the same way but do not carry stocks of goods. Although manufacturers' branch houses perform services similar to the independent wholesalers, they usually carry only goods made by their owners. Consequently, they do not offer the retailers as wide a selection of goods as do independent wholesalers. The policies of manufacturers' branch houses are determined by the main office. Some houses pass on credit while others refer credit purchases to the main credit office for approval or rejection.

Chain store warehouse operations resemble those of independent wholesalers selling similar goods except that the former have no salesmen. The chains buy from manufacturers (sometimes through brokers), warehouse the goods, assemble the orders received from their retail stores, and deliver the goods to these stores in their own trucks, by rail, or by outside truckmen working under contract. The managers of the retail stores in the chain requisition goods for deliveries which are made to them on schedule. As chains seldom operate very small stores, few orders are received for less than case lots. Packages are seldom opened, divided, and repacked. Because the number of deliveries is limited, trucks follow designated routes and go out fully loaded. These and similar economies usually enable chain store warehouses to have somewhat lower operating expenses than the cash-carry and retailer-owned wholesale houses. The more efficiently operated retailer-owned and cash-carry houses, however, have costs as low as the chain store warehouses.

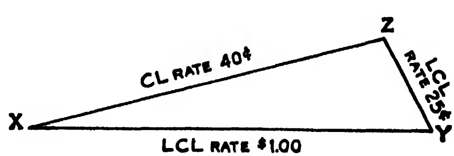
The majority of chain store warehouses are operated by gro-

cery and drug organizations. These are convenience goods normally handled by wholesalers. When chains enter the field they find warehouses necessary. The same is true of hardware and auto accessories but there are fewer chains in these lines. In other trades, chains operate relatively few warehouses as most goods are shipped direct to the retail stores by the factories. The chain buying offices contract for the goods and notify their store managers who requisition the goods as needed. The packing, shipping, and billing of the orders to the chains' retail stores increases the expenses of the manufacturers over shipments to wholesalers or chain store warehouses.

Services Performed by Wholesalers

For manufacturers. Wholesalers provide sales organizations to sell the manufacturers' goods to the retailers. But for this, each manufacturer would have to maintain his own sales force contacting retailers, which would greatly increase the number of salesmen needed and thereby increase the cost of marketing goods. In 1939, there were seventeen times as many retailers as wholesale merchants, and twelve times as many retailers as wholesalers including manufacturers' branch houses and sales offices, and bulk tank stations. A manufacturer might need twelve times as many salesmen to sell the retailers as to sell the wholesalers.

The wholesalers provide warehouses in order to keep stocks of goods close to the retailers. If we had no wholesalers, the manufacturers would need to carry larger regional stocks. Carrying stocks close to the retailers often saves transportation costs because goods are moved long distance at carload rates and short distances at less-than-carload rates. (See the following diagram.) The goods are produced at X and consumed at Y. The retailer at Y cannot use a carload at one time. If he buys from the manufacturer, he will pay the l.c.l. freight of $1 per



100 pounds. A wholesaler is located at Z. The carload rate to Z is 40 cents and the l.c.l. rate from Z to Y is 25 cents. Thus the total freight cost in having the goods shipped to Z in carloads and from Z to Y in less-than-carloads is 65 cents. The differential is often of great importance, especially on heavy staple goods where competition is keen.

The manufacturer can often save the same amount by having the goods stored in a public warehouse at Z, if one is there. Good public warehouses will receive the goods, place them in storage, divide them and ship in small lots on order of the manufacturer. At times the manufacturer will give the warehouse a list of customers who may requisition goods from stocks in the warehouse without having their orders approved by the manufacturer's credit department. The warehouse in this case becomes a competitor of the wholesaler. It does not, however, perform many of the wholesale functions. The manufacturer distributing to retailers through public warehouses must have his own sales organization, extend credit, keep books, make collections, and supervise the distribution of warehouse stocks.

The wholesaler divides the large shipments received from the manufacturer, assembles the orders requested by retailers, and delivers or ships the goods to the retailers. Invoices must be made and records kept of accounts with retailers. To pack, ship, and account for many small orders would increase the manufacturer's expenses.

The wholesaler extends credit to the retailers and makes collections. Most retailers are small and have limited capital. Extending credit to, and making collections from thousands of small retailers is a most difficult problem for the manufacturer. The wholesaler can perform this function at a reasonable cost because he is close to the retailers, his salesmen call on them frequently and he can supervise collections.

The wholesaler receives much information from the retailers about the demand of the consumers and their likes and dislikes. He passes this information back to the manufacturers who often find it very valuable.

The wholesaler, by assuming the risk involved in storing

goods and selling on credit, relieves the manufacturer of this responsibility.

For retailers. The wholesaler gives the retailer a nearby source of goods. Many retailers have limited capital, have inadequate stock control systems, and so buy frequently and in small quantities. It is safe to say that without the wholesaler a great many of the small retailers would find it impossible to stay in business.

The wholesaler also extends credit, an advantage to most retailers who have limited capital and buy on credit, and especially so if they sell on credit. As explained above, many manufacturers find it extremely difficult or expensive to extend credit to small retailers.

The wholesaler's salesmen not only solicit orders, thus saving retailers the trouble of originating their own, but also give the retailers much information and advice; for example, they tell what goods are needed and how to display and price them. This is particularly helpful to new and inexperienced retailers.

Expenses of Wholesale Merchants

The expenses of individual wholesalers vary with the method of operation and services rendered, and with the efficiency of operation. The wholesaler who gives free delivery and sells on credit usually has higher expenses than the cash-carry wholesaler. Similarly, the wholesaler who carries stock has higher expenses than one who does not perform the warehousing function. Wholesalers who carry large and complete stocks have higher expenses than those with small stocks of fast-moving goods. The wholesaler employing salesmen will have higher expenses than one with no salesmen. The service wholesaler has outside salesmen. The cash-carry wholesaler must have house salesmen to take orders from retailers who visit his warehouse. The chain store warehouse receives orders from its retail store managers and needs no salesmen. The retailer-owned and voluntary wholesaler may receive many orders by mail but must employ some order takers to receive telephone requests. The wholesaler who receives many orders which involve break-

ing packages and assembling a variety of items into orders will have relatively higher expenses than the wholesaler who receives very few small orders.

The efficiency with which the wholesaler manages his business may be of equal or even greater importance than his method of operation. There is a very great difference in the expense percentage of wholesalers handling similar goods in the same territory. In one territory a cash-carry grocery wholesaler had expenses of over 8 per cent while a cash-delivery wholesaler had expenses of less than 6 per cent. One voluntary house may have expenses of 12 per cent while another has expenses of only 4 per cent.

At this point we cannot undertake an analysis of the factors required for efficient operation. It involves such matters as volume of sales per salesman; number of orders assembled per day by each order picker; layout of delivery routes and sending trucks out with full loads; promptness with which customers are induced to pay their bills; the way goods are handled in the warehouse; and purchasing methods that prevent shortages and overstocks. Efficiency of operation also depends upon morale of employees, type and layout of warehouse, and the equipment used.

Size and expenses. Wholesaling is an industry of decreasing costs: the expense percentage decreases as the volume of sales increases. This is true in most trades. However, in certain trades the optimum sales volume, or point of lowest expenses is soon reached. Wholesale grocers with sales between $200,000 and $300,000 have lower expenses than either larger or smaller houses. With drug, hardware, and electrical wholesalers, expenses decline very little when sales increase beyond $300,000. The expenses of oil well supply houses and several other types of wholesalers, however, show a greater tendency to decrease as sales increase and cause the average of all trades to decrease with size.

The decreasing expenses would apparently concentrate business in the hands of relatively few large wholesalers, but this is not the case. Eighty-five per cent of all wholesale merchants had sales of less than $300,000 and 44 per cent had sales of less

TABLE 6–2

RATE OF EXPENSES OF WHOLESALE MERCHANTS, 1939: PERCENTAGES OF SALES

(Census Figures)

SALES VOLUME (Dollars)	ALL TRADES		SELECTED TRADES				
	Number	Expense	Groceries	Drugs	Hard-ware	Electri-cal	Oil-well Supplies
Total and Averages	92,794	13.7	9.6	13.4	18.3	13.4	10.5
Under 50,000	40,484	21.7	12.7	—	21.0	20.0	24.5
50,000 to 99,000	16,971	19.3	9.7	19.1	24.8	16.4	19.6
100,000 to 199,000	14,226	17.9	9.4	13.6	22.4	15.8	12.4
200,000 to 299,000	6,717	16.1	8.7	15.0	21.0	14.1	10.7
300,000 to 499,000	6,195	14.9	8.9	13.8	19.0	13.1	8.9
500,000 to 999,000	5,047	13.5	9.0	13.1	19.0	13.1	7.0
1,000,000 to 1,999,000	2,052	12.3	9.7	13.1	18.3	13.8	7.2
2,000,000 and over	1,102	8.9	12.1	13.3	17.5	13.0	9.5

than $50,000 in 1939. Such wholesalers are small compared with many manufacturers, department stores, and chain stores. Thus we find that, despite decreasing costs, wholesaling is essentially an industry of small operators. Prior to the war boom, only two wholesalers recorded sales of over $100,000,000 and these operated chains of warehouses.

Because the retailer wants his goods as quickly as possible after he places an order, the nearby wholesaler has an advantage over those at a greater distance. This has led to a great increase in local wholesalers. To illustrate, in 1900, 25 towns in Illinois had wholesaler grocers; in 1929 there were 76 such towns. Another illustration: in 1931, 264 towns in the United States had electrical wholesalers and in 1943 there were 457 such towns. There are few trading center towns of over 4,000 without at least one wholesale grocer.

The local wholesaler is closer to his customers, calls on them more frequently, has closer personal relations with them, and can make quicker deliveries than the wholesaler located at a distance. As a result, he may be able to operate profitably even when he has slightly higher expenses.

A very large proportion of wholesalers, perhaps one half of the total, are one-man, one-family, or two-family concerns. In such businesses the proprietors may not distinguish between salaries and profits but strive to make a living rather than to earn a profit. If they make enough to support their families they may be satisfied, at least until their businesses grow.

Place of the Wholesaler in Distribution

Scarcely had the wholesaler established himself in the trade channel when some people began to say that he was an unnecessary middleman and should be abolished. Certain factors have tended to lessen his importance: when manufacturers become large they often sell direct to the retailers either through their own salesmen, or by establishing their own branch wholesale houses; when retailers become large they tend to buy direct from the manufacturers. This shift is true of department and chain stores, both of which are important.

The number of wholesalers has continued to increase, however. From 1929 to 1939, the number of wholesale merchants increased as follows: Service wholesalers from 74,612 to 94,350, and limited function wholesalers from 2,156 to 4,533. From 1935 to 1939, the number of agents and brokers increased by almost 3,500; the number of farm products assemblers by more than 2,000; the number of manufacturers' branch houses by almost 1,500 and the number of branch sales offices by approximately 900.

The wholesaler could not survive unless he performed necessary functions. Convenience goods are sold chiefly by small retailers situated close to the consumers. Since it is usually impracticable for these retailers to buy direct from factories, the goods must be warehoused nearby. This warehousing may be done by wholesale merchants, by manufacturers' branch houses,

or by retail warehouses operated by chain stores or groups of independent retailers. Although wholesale warehousing by manufacturers and retailers has grown, the independent wholesaler is still extremely important. He performs functions that are valuable to both manufacturers and retailers. He is increasing in number and holding his own in sales volume but appears to be declining slowly in relative importance. The question is: who can perform the wholesale functions to best advantage—the independent wholesaler, the manufacturer, or the retailer?

Old wholesale houses quit business or merge with others. New houses come into existence. Individual wholesalers come and go but wholesaling continues.

Questions

1. What are the two main classes of wholesalers? Distinguish between them.
2. How does the service or full-function wholesale merchant operate?
3. Explain how a drop shipper operates?
4. In what trade is the cash-carry wholesale merchant most prominent?
5. What is a converter?
6. Is there any difference between the service-type wholesale merchant and the industrial distributor? If so, what?
7. Who takes the initiative in forming a voluntary group? How does such a group operate? What is the main advantage to a retailer in belonging to such a group?
8. How is a retailer-owned wholesale house operated?
9. What is an integrated wholesale house? What are the three types of such houses?
10. What services do wholesale merchants perform for manufacturers? For retailers?
11. Explain how a wholesale merchant makes savings in transportation cost possible.
12. What factors affect the expenses of wholesale merchants?
13. Why is the business of a wholesale merchant a business of decreasing costs?
14. Will the wholesaler be eliminated from trade channels?

7

The Manufacturer and His Outlets

A MANUFACTURER may (1) turn over the sale of his product to a selling agent, (2) sell through manufacturers' agents to wholesale buyers, (3) sell direct to wholesale buyers with his own salesmen, (4) sell direct to the retailers, or (5) sell direct to the consumers. If he sells to wholesalers or retailers, he may sell from his home sales office, from branch sales offices, or from branch houses which carry stocks of goods for immediate delivery. If he sells to the consumers he may sell through his own retail stores, through house-to-house salesmen, or by mail.

Important factors affecting the manufacturer's choice are the type of goods he has to sell; whether he has a full line or a single product; whether his product has much or little consumer demand; the territory he covers; and his capital and sales ability.

Convenience goods are sold by city, small town, and rural stores. They are sold by large and small stores but a very large proportion are sold through small stores located in outlying neighborhood retail districts in large cities, in suburban towns, in small towns, in villages, and along our highways. These stores must buy in relatively small quantities and most of them want frequent deliveries. Therefore a very large quantity of these goods are sold through wholesalers including chain store warehouses and bulk tank stations.

Fashion goods are sold principally in larger stores concentrated in the shopping centers of our trading center towns and cities. These buy in relatively large quantities. Many fashion

goods are highly perishable owing to the risk of change in style. They should reach the retailer quickly. Others, like furniture, are bulky so that handling through a wholesale warehouse is expensive. For these reasons, the great majority of fashion goods are sold to the retailers by the manufacturers or by their agents.

The larger industrial goods are usually sold direct to the users, although many are sold through agents. Many of the smaller goods are sold through wholesalers called industrial distributors or mill supply houses.

Choice of Outlets

If he knows the type of product he is selling, the manufacturer can usually choose his outlet and determine the type of retailers best adapted to its sale. Getting these retailers to handle his product may, however, prove difficult. The retailers may already have full stocks, or have no interest in a new brand unless it has considerable consumer demand. A manufacturer who finds the logical outlets full of competing products may place his wares in another type of outlet or sell direct to the consumers. We have seen phonographs, radios, electric irons, automobile tires, and silk hosiery offered for sale in drugstores. Toys, porch furniture, garden equipment, and lawn furniture are sold in tire and automobile accessory stores, and house dresses offered in grocery stores. Placing goods in a new type of outlet is not always successful; when contemplated, the new outlets should first be tried out with caution.

Borderline products. Many products are on the border between two classes and may be sold through several types of stores. Work clothing, for example, is sold by grocery, general, clothing, and department stores. Cheap jewelry, low-price cosmetics, toys, paint, and kitchen utensils are bought by some people as convenience goods and by others as shopping goods. Producers of such articles may sell them through more than one type of outlet.

Full-line versus specialty manufacturer. The seller with a full line of products is more likely to sell direct to the retailers

than is the seller of a single product. Selling expense is likely to be too high to allow the short-line manufacturer to sell direct to retailers. On the other hand, a seller with a full line or family of products may secure a large enough volume to sell the retailers economically. Full-line canners, packers, bakeries, and farm implement manufacturers frequently operate their own branch houses while short-line manufacturers sell to wholesalers. The same is true of manufacturers of high value items such as tires or household appliances.

Consumer demand. The salesman whose product is in general use and has general consumer acceptance can secure more and larger orders per day than can the salesman for a new or unknown product of the same quality. The well-known product is handled by most dealers, so the salesman will get orders from most of the stores on his route. Since the product is a good seller, his orders will be larger than for an unknown product. Thus the seller of a widely used product may have selling expenses low enough to enable him to sell direct to the retailers while the seller of a new product, or one new in the territory, cannot afford to do so, except temporarily to introduce it.

Territory covered. In densely populated areas where buyers are close together a manufacturer may be able to sell direct to the retailers, but one selling in sparsely populated areas will find it more profitable to sell through wholesalers. A manufacturer who sells in both types of areas may sell direct to retailers in metropolitan areas and to wholesalers in rural areas. Some wholesalers do not like to handle goods of producers who use both methods; they fear that after they have introduced the line the manufacturer will cancel the agreement and have his own salesmen call upon the retailers.

Some manufacturers sell the larger buyers (downtown stores, for example) and leave the small buyers, such as neighborhood stores, to the wholesalers. The wholesaler may be able to sell the small retailers profitably since he sells many products. For example, orders for less than $25 may be unprofitable. The manufacturer would lose money on sales of single items valued at $1 or $10. The wholesaler, however, can combine these with other merchandise, secure larger orders, and so operate

profitably. Naturally the wholesalers do not like the arrangement that gives them only the small orders. They may refuse to handle the goods of manufacturers following this policy. If the manufacturer's product is in wide demand, the wholesalers may need the product; if so, wholesalers cannot refuse to handle it, but they probably will not push the product under these circumstances. The manufacturer who wants the whole-hearted co-operation and support of the wholesalers should give more consideration to the wholesaler's point of view.

In cities, salesmen often live at home and their employer does not have to pay their traveling expenses. Salesmen in rural areas usually have their expenses paid and sometimes their expenses are more than their salaries. Some city salesmen calling upon small retailers receive a straight salary which includes a small expense allowance; others have all their expenses paid. One study showed average expenses of city salesmen to be $612 and country salesmen to be $1,599. Total average remuneration (salary, commission and expenses) was $2,913 in cities and $4,135 in the country.

A country salesman not only costs more than a city salesman but owing to the distances between dealers, he makes fewer calls per day. A salesman's rural orders may be larger than his city orders because fewer salesmen call on country retailers, who consequently may buy in slightly larger quantities.

Some of these factors may be illustrated by two manufacturers selling direct to retailers in both urban and rural territory. One is a full-line house with a well-established line and the other is a short-line house whose product is not widely used in the territory.

As the salesman for the full-line house has more items, he can make fewer calls per day than the salesman for the short-line house. However, since his line is favorably known and widely used in the territory, he can sell a larger proportion of his prospects. Because he has many items to sell, his orders are large. The direct selling expense for the city salesman is 2.9 per cent, probably a little higher than that of the wholesaler's salesman. This is a reasonable expense for most products. The manufacturer can successfully sell direct to retailers if he can

warehouse, deliver to the retailers, and handle their credit. The direct selling expense for the country salesman is 5.0 per cent. Some products will bear this expense and some will not. If the manufacturer has staple and highly competitive products, he may use the wholesaler to contact the country merchants; his own specialty or missionary salesmen may then call on these retailers two or three times a year.

TABLE 7–1

COMPARISON OF SELLING EXPENSES OF FULL-LINE AND SPECIALTY MANUFACTURERS IN URBAN AND RURAL TERRITORY *

	FULL LINE MANUFACTURER		SPECIALTY MANUFACTURER	
	City	Rural	City	Rural
Salary and bonus of salesmen	$3,600	$3,600	$3,600	$3,600
Expenses of salesmen	800	2,400	800	2,400
Total expense per salesman	$4,400	$6,000	$4,400	$6,000
Number of calls per day	16	10	22	12
Number of sales per day	12	8	9	6
Average size of sale	$50	$60	$12	$15
Sales per day	$600	$480	$108	$90
Annual sales (250 days)	$150,000	$120,000	$27,000	22,500
Percentage, direct selling cost	2.9%	5.0%	16.3%	26.7%

* Typical figures for 1945–1946.

The salesman for the short-line house can make more calls per day because he has fewer articles to sell. As his product is relatively unknown and does not have wide consumer acceptance in the territory, he makes fewer sales per day. Because he has fewer items to sell, his orders are smaller. The direct selling expense for the city salesman is 16.3 per cent. If the manufacturer's line carries a wide margin he may be able to afford this expense, at least temporarily, while introducing the product in new territory. On the other hand, if he has a staple product with a narrow margin, he cannot afford to keep his salesmen in the cities. Instead, he may temporarily use specialty men who turn their orders over to the wholesalers. Since his country

sales expenses are prohibitive, the manufacturer will have to depend upon the wholesalers to reach this area.

Capital and sales ability. The well-established manufacturer with plenty of capital is more likely to sell to the retailers than is the new manufacturer with limited capital. The manufacturer with sales experience is more likely to sell direct to the retailers than is the manufacturer whose experience has been in production. The latter often feels that he can more profitably devote his attention to production matters—reducing costs or improving quality—and leave the marketing of his product to others who are experienced and skilled in this field.

Selling to a Few Large Buyers

Some manufacturers prefer to concentrate on production and leave the marketing of their goods to others. They reason that they know more about production than marketing and will do better to concentrate on it and leave marketing to experts in that field. They feel that they can make more profit by increasing their productive efficiency than by dividing their efforts. There is much to be said for this position, if the manufacturers succeed in finding satisfactory outlets for their goods.

A large hosiery manufacturer maintains one sales office in New York and sells to chain and department stores under their own brands. He makes hosiery of various kinds and qualities to suit the buyers. When asked about establishing his own brands, he says: "Advertising is all right; but not for us. We have a large and profitable business and are satisfied with it." A vegetable canner who operates several large plants and cans a variety of products follows much the same policy. He has no brokers and no salesmen. He and his sales manager sell by mail, telephone, and by personal visits to wholesalers, chain stores, and institutions. Most of his goods reach the consumers under the brands of the buyers but he has several brands of his own which are used when the buyers desire. He holds his costs down and follows a one-price policy. He finds his business satisfactory and has no thought of changing his method of distribution.

When there are a number of buyers, the policy of selling to a few large concerns under their own brands may be successful, but selling the entire output to one buyer or a very few buyers is often disastrous. A dress manufacturer tripled the size of his plant to make dresses for a large chain. Within two years another manufacturer offered equally good dresses at lower prices and took the contract. The first manufacturer was forced into bankruptcy, an all too common occurrence when a producer has only one customer. The producer with but two or three customers is also in a precarious position. The manufacturer without a sales organization or an established brand should have several customers as well as several other prospects available in case he loses a contract.

An overall manufacturer sold his entire output to a large chain. Overalls are sold on narrow margins by both producers and distributors. The factory was located in a town with relatively low wages and was operated efficiently. He had no sales expense as he had only one contract to negotiate, and no credit department because the chain paid bills promptly. Although satisfied with his profit, the manufacturer was constantly in a state of uncertainty; he never knew when another manufacturer might underbid him. To guard against this contingency, he put his own name on some of the overalls and hired salesmen to contact the retailers. Selling expenses were so high, however, that his price was above the retail price of the chain. The manufacturer then made a drastic change in policy. He made a different garment and advertised it extensively to the consumers. He now has many more marketing problems but his business is more secure.

Developing Consumer Acceptance

Consumer acceptance for a product may be developed by personal salesmanship, by retail store displays, or by advertising. Widespread consumer demand for Hershey candies and Fruit-of-the-Loom dry goods, for example, has been created by their quality, by the name on the product, and by store displays. Most products that have won wide consumer acceptance have

used advertising extensively. Cream of Wheat is an example. Sellers frequently use a variety of means—advertising, specialty salesmen, store displays, window displays, premiums, contests, and demonstrations.

Benefits of consumer acceptance. The seller who secures widespread consumer goodwill for his product will have larger sales and perhaps slightly higher prices than are received for less widely-known items. If a product is in great demand, wholesalers and retailers may sell on narrow margins; the producer then receives a higher price without any increase in consumer prices. At times the margin is so small that distributors lose interest in the product and place their own brands on the market in order to increase their margins. We hear and read much about the competitive battle between manufacturers' and distributors' brands.

Distributors' brands. Many wholesalers, chain stores, department stores, and mail-order houses have their own brands. The small retailers usually do not, unless they are members of retailer-owned co-operative wholesale houses. Distributor's brands are found on almost all types of goods, but perhaps are most common on grocery, drug, toilet, and cosmetic items. Some distributors' brands are very well known in the territories where they are sold. Many have secured goodwill and acceptance through use and by display in retail stores. Others have been widely advertised. Several well-advertised lines of cosmetics are those of distributors. When a distributor sells goods under his own brand, he is in direct competition with the manufacturer making similar goods. If the distributor handles both his own and the manufacturer's brands (as frequently happens), the manufacturer fears that the distributor favors his own line. This is sometimes the case, but the distributor says that he would prefer to push the manufacturer's brands if they provided satisfactory profits. To develop his own brands involves expense and risks. He must find satisfactory sources, negotiate contracts, inspect the goods, buy in large quantities, and develop a demand for goods under his own brand.

The reasons for a distributor handling goods under his own brand name are that he can buy them cheaper and earn a larger

margin on sales. Since he controls the selling price he can take a wider margin or undersell the manufacturer's nationally advertised product; often he does both. The distributor owns his brand and any goodwill attaching to it benefits him. No one can take the brand away from him. After he has spent years building up the manufacturer's sales the latter may decide to sell his product through exclusive agencies. Or, if the distributor is an exclusive agent, the manufacturer may sign an agreement with another. In the case of the wholesaler distributors, the manufacturer may decide to sell direct to the retailers.

The manufacturers' brands. The manufacturer with a nationally advertised brand maintains that his brand is widely and favorably known, that the consumers prefer it, and that owing to a ready-made demand, the wholesalers and retailers can sell it with less expense than their own brands. Thus, he argues, the national brand is more profitable to the distributor even with a lower margin. Not enough information is available to refute his opinion, but many distributors are not convinced by it. They say that in many instances there is too much difference in profit margins. Although distributors' brands may not be nationally advertised, many of them are generally accepted by the consumers in territories where they are sold. In fact, certain distributors' brands of food products have more consumer acceptance than many of the manufacturers' nationally advertised products. This is less commonly true of drug and toilet articles.

The national advertiser says that his products are of better quality than the distributors' private brands. He maintains that handling goods under national brands creates prestige for the store and attracts customers. The latter argument contains considerable truth; there are few retail stores that do not carry some national brands. Self-serve stores often favor nationally advertised brands because the goods must sell themselves.

The consumer's interest in brands. The consumer is interested in quality and price. We do not have enough information to make any general statement as to the relative qualities of nationally advertised and distributors' less widely advertised brands. The national advertiser says that he cannot afford to let his quality deteriorate after putting so much money in his

advertising. The distributor, however, says that his goods are of better quality for the reason that he can change his supply source if a producer starts delivering poor quality merchandise. Studies of the quality of canned fruits and vegetables have shown that the quality of distributors' brands is fully as good as manufacturers' brands.

There is more information on prices and it indicates that consumers can buy distributors' private brands at somewhat lower prices than nationally advertised brands. The data include the costs and selling prices of various drug and grocery items. The price to the wholesaler of the widely advertised product is taken as $1 and the other prices compared with it. The competing brands include both distributors' private brands and manufacturers' products that are not nationally advertised. The consumer price of seldom advertised brands of drugs is about 16 per cent lower, and groceries almost 11 per cent lower, than that of the widely advertised product. Both wholesalers and retailers have substantially higher margins on the distrib-

Table 7–2

WHOLESALERS' AND RETAILERS' COSTS, PRICES, AND MARGINS ON NATIONALLY ADVERTISED AND COMPETING BRANDS OF DRUGS AND GROCERIES *

	Drugs		Groceries	
	Widely Advertised Brands	Competing Brands	Widely Advertised Brands	Competing Brands
Cost to wholesaler	$1.00	$0.60	$1.00	$0.85
Selling Price to retailer	1.15	.73	1.13	.99
Selling Price to consumer	1.67	1.41	1.45	1.31
Margins: Wholesaler per cent of selling price	13.3%	17.8%	11.4%	13.9%
Margins: Retailer per cent of selling price	30.9	47.9	22.0	24.9

* Adapted from reports of the Federal Trade Commission: Resale Price Maintenance, Part II. Competing Brands are those of distributors and manufacturers who do not advertise widely. The cost of the nationally or widely advertised product to the wholesaler is taken as $1 in each case and the other prices compared with it.

utors' than on the national brands. It is doubtful, however, if handling expenses for the two types differ as much. If not, their percentages of profit would be higher on the distributors' brands.

Development of a Manufacturer's Sales Methods

Let us trace the sales methods used by a manufacturer who begins with little capital or business ability. A man is mechanically inclined and invents a good product, raises a little capital, and begins production. Perhaps a group of men, in order to increase employment in the town, raise some money, build a plant, and hire a foreman from another factory as plant manager. In neither case does the manager know much about marketing. These companies are very likely to turn the marketing of their product over to a selling agent and have him sell their entire output. He may also help to finance the plant by endorsing their notes or loaning them money when working capital is needed.

The arrangement may prove desirable for a time if the cost is low or if the product is distinctive. If the company is successful, profits are reinvested and the plant is expanded. Sooner or later the producer wants more volume, a higher price, or both. He feels that the selling agent is not actively promoting the sale of the product. He may therefore dismiss the agent and contract with manufacturers' agents in various markets. The producer visits their offices occasionally, and exercises general supervision over his agents. Sales increase and for a time he is satisfied.

When he wants greater volume, he may create his own sales organization and have his men sell to wholesalers. Sales increase rapidly while the wholesalers stock up, and then they decline. It takes considerable time for the wholesaler's salesmen to learn that the new product is in stock and to mention it to their customers; several months may elapse before they turn in sizable orders. When they do, the manufacturer's sales increase, the wholesalers restock his goods, and pay for the goods promptly. The producer may be satisfied for several years but

eventually he desires an even greater volume of sales. Since the wholesalers carry several competing lines, the producer feels that their salesmen do not push sales but only take the orders given them by the retailers. Consequently, he may try consumer advertising. This increases his sales but, having an advertised product, he feels that his sales volume should increase still more.

To sell the retailers direct would involve a much larger sales organization; carrying regional stocks; packing, shipping, and invoicing many small orders; extending credit to many financially weak retailers; making collections; and a lot of detailed bookkeeping. The producer is not willing to undertake a program which would require a greatly enlarged organization and additional capital, but he wants increased sales. He feels that the wholesaler does a good job of warehousing, shipping, bookkeeping, and credit extension but a poor job of selling. To improve the situation he hires a force of specialty or missionary salesmen to work with the wholesalers' representatives to increase the sales of his product.

Specialty salesmen. These missionary salesmen call upon the retailers and sometimes travel with the jobbers' salesmen. They present the product and try to educate the retailer as to its good qualities and method of sale. They persuade the dealer to display the product on his counters and in his windows, and may wash the dealer's windows and arrange window displays. They give the retailer display cards advertising the product, solicit orders for the product, and turn these orders over to the wholesaler who delivers the merchandise and collects payment. Specialty salesmen increase sales, but the larger volume hurts the sales of competitors who reciprocate by hiring their own specialty salesmen. If all have specialty salesmen, our manufacturer secures no advantage from their services.

To gain an advantage, the manufacturer ships stocks of goods to public warehouses, thus enabling him to make prompt delivery direct to retailers when the wholesalers are out of stock. The wholesalers soon find this out and are not pleased. The manufacturer is soon filling most of the orders direct from his warehouse stock: dividing the goods, packing for reshipment,

and issuing invoices which are turned over to the wholesaler for collection. The manufacturer is now performing the selling, warehousing, dividing, and shipping functions. The wholesalers perform only the credit and collection bookkeeping functions, provide the capital, and take the risk on accounts. The wholesaler's margin has been reduced and he has lost most of his interest in the product. The manufacturer considers if he can profitably extend credit and make collections and so dispense entirely with the services of the wholesalers. His own salesmen would devote full time to increasing the sale of his product. With his own salesmen the manufacturer can work more closely with the retailers and secure more co-operation in sales programs. He will probably find that it costs more to operate without the wholesaler's services. Even though his marketing expenses increase, his profits may show a satisfactory increase in total amount if not in percentage.

Dispute over use of specialty men. The manufacturer, when he helps the wholesaler sell a product, feels that the wholesaler should reciprocate by having his salesmen actively push sales. The manufacturer also feels, since he does much of the selling, the wholesaler should handle the product on a smaller margin. On his side, the wholesaler often complains that the product is handled at a loss because the margin is so low. Many of the products sold by specialty salesmen are widely known articles with strong consumer demand. Such products are often used as leaders by the retailers. In order to prevent a loss, retailers try to buy the products at low prices. The wholesaler's price is often pushed so low on these promotional articles that he makes little or no profit and naturally loses interest in them unless they help him to sell other merchandise. The wholesaler prefers to sell other brands offering wider margins, or to promote goods under his own brand name.

As in most disputes, many minor complaints are advanced on both sides. Wholesalers claim that many of the specialty salesmen "high-pressure" the retailers into buying, overstock them, and send in forged orders which the retailers refuse to accept on delivery. The manufacturers answer this charge by requiring their salesmen to obtain the retailer's signature on all orders.

The manufacturers claim that the wholesaler's salesmen ask the retailers to cancel the orders secured by the specialty men and to substitute other brands carrying wider margins. The wholesalers deny this allegation. When the specialty salesman travels with the wholesale salesman, it is alleged that the latter's work is hindered because he must wait for the specialty man to talk with every merchant. So the dispute goes. There are, however, many cases of real co-operation between the wholesalers and the manufacturer's specialty men.

Summary on services of the wholesaler. Some type of wholesaler is necessary to distribute convenience goods which are sold mainly by small retailers unable to buy direct from the manufacturers. Chain stores handling convenience goods establish their own wholesale houses. When manufacturers sell direct, they usually find it necessary to operate their own branch houses, or carry regional stocks in public warehouses.

Generally, manufacturers can reach the retailers more economically through wholesalers than by setting up their own sales organizations. Manufacturers set up their own sales organizations when they become dissatisfied with the volume of sales made by the wholesalers. Their main criticism of the wholesaler is that he does not push the sale of their goods, that he does not "create demand."

The wholesaler is primarily a purchasing agent for the retailers and not a salesman for the manufacturers; the wholesaler could not exist without retail customers. It is therefore to his interest to help the retailers operate their stores profitably; they need information, advice, and prices that will enable them to resell the goods in competition with chain and other stores.

Exclusive Agencies

The manufacturer may grant exclusive agencies or territories to wholesalers or retailers in order to secure their interest in his goods and induce them to push sales.

Wholesale exclusive agencies have been tried and in some instances the result has been a doubling, tripling, or quadrupling of sales volume. Having no competition from other whole-

salers in his territory, the wholesaler with an exclusive agency instructs his salesmen to push the line. He uses the manufacturer's promotional material, often has the manufacturer's sales manager address his salesmen, instruct them in the construction and use of the product, and "pep" them up on its sale.

The difficulty with exclusive territories is that areas of different wholesalers overlap. Suppose that an exclusive agency is granted to three wholesalers in Indianapolis, Chicago, and St. Louis. All three houses have salesmen covering central Illinois. Under exclusive territory rights only one can sell the product in this area; the other two cannot sell the product in central Illinois. They will lose sales or push other lines. Hence the wholesaler will carry more than one line since his salesmen cannot sell the exclusive line in all his territory.

Confined lines are used to prevent this situation. The manufacturer gives his product to only one wholesaler in each of the three cities, and each wholesaler sells the line in all the territory he covers. There is some overlapping of territories, but the arrangement is practical for the manufacturer as he secures substantially the same interest from the wholesaler as if the latter had the exclusive right to sell the product within a definite area.

Exclusive retail agencies. Some manufacturers grant exclusive territories to retailers. This is done to secure the better dealers as agents, to provide the dealers with complete stocks, and to encourage sales by furnishing personal salesmanship, displays, advertising, and other helps. The retailer who is an exclusive agent for a product knows that no other dealer in the town can sell it and feels justified in putting special sales effort behind the line. He is relieved of the danger that some other dealer will cut the price, forcing him to do likewise and so reduce his margin. If the line is well known it creates prestige for the store and brings customers who may buy other goods also. Thus, the agency for a popular line may increase sales of other lines. When a manufacturer grants an exclusive agency, he may co-operate with the retailer in several ways. He may (1) provide advertisements and pay part of the cost; (2) instruct the retailer's salesmen in ways of selling the product; (3) help the dealer arrange store and window displays; and (4) provide a stockkeep-

ing system. Retailers are anxious to obtain exclusive agencies for popular lines and are willing to devote special sales effort to the line in order to secure and hold the agency privileges.

The manufacturer selling through exclusive agencies may be able to secure better outlets than he could otherwise. Retailer interest in selling his goods is greater. He may be in a position to demand that the dealers carry complete stocks, advertise his goods, display them in the store, and maintain the established prices. He has fewer dealers and therefore employs fewer salesmen. Because the number of accounts is small less bookkeeping is necessary; if his dealers are financially sound, his credit risk is reduced and payments more prompt.

Limitations on use of exclusive agencies. The test of selling successfully through exclusive agencies is whether or not the method increases sales for the manufacturer. The argument in favor of exclusive agencies is that a limited number of good stores actively pushing sales will sell more than a much larger number of stores who do not push the line. In some cases this is true. In many cases this is not true, however. Sales usually vary with the number of salesmen and outlets handling a given line. Several stores will sell more than a single store.

Exclusive agencies have little place in the sale of convenience goods. The manufacturer of such goods wants the largest possible number of outlets for his product: downtown stores, neighborhood stores, trading center stores, village stores, and stores along the highways. It may, however, be good policy to grant exclusive agencies for convenience goods when a new sales territory is being opened. In fact, it may be the only way to secure dealer interest. The exclusive agency contract usually allows either party to cancel the contract upon notice given a specified time in advance. Thus, exclusive agents may be used to introduce a product and given up when more stores can be induced to stock the item.

Exclusive agencies are most commonly used in the sale of service goods: household appliances, automobiles, farm implements, and the like. They are sometimes used with fashion goods such as shoes and men's suits. It is impractical for the

small or medium-sized shoe store to carry many lines, for example, owing to the number of sizes and lasts.

It is difficult to use exclusive agencies in a large city unless the contract is given to a chain that has stores in all parts of the city. No one store, not even a downtown department store, can cover adequately an entire city for a widely used good. In large cities the manufacturer may, however, confine his line by giving it to only one store in each shopping district.

Legality. It is legal for a manufacturer to grant the exclusive right to sell his product in a given territory. However, it is not legal for the retailer to agree not to handle competing lines. Such an arrangement would limit the selling opportunities of other manufacturers and so be a restraint of trade.

Selling Direct to Consumers

The manufacturer may sell to the consumers in three ways: by establishing his own retail stores; by using house-to-house salesmen; and by mail or radio advertising.[1] The operation of retail stores by manufacturers will not be discussed here since their operation involves all the problems of store operation which are covered in later chapters. As a rule, the operation of chains of retail stores by manufacturers is none too successful. Retailing problems are quite different from those of manufacturing. Few companies have the skilled management for both. There are, of course, notable exceptions: candy makers, shoe factories, and manufacturers of men's clothing. These may be the "exceptions that prove the rule." Many manufacturers, however, operate one, two, or three retail stores as laboratories in which to study the retailing of their products. The information obtained and methods developed are passed on to the retailers who sell the merchandise.

House-to-house salesmen. Manufacturers may sell from house to house either by having salesmen operate trucks and deliver as

[1] Farmers may sell direct to consumers by peddling from house to house; displaying their goods in farmers' markets; by setting up roadside markets or by mail solicitation.

they sell, or by having salesmen solicit orders for later delivery. The latter method is used more frequently. Many kinds of products, especially new ones which the retailers are unable or unwilling to introduce, are sold from house to house by specialty salesmen. Some are novelties or specialties which are not used widely enough to be stocked by retailers. Some items, such as nursery stock or machinery, are unsuited to over-the-counter sale. At times a newcomer finds the retailers uninterested in an additional product. He may not have the money for creating consumer demand by extensive advertising and so hires specialty salesmen to solicit consumer orders. In this way he can start selling in a small area and expand his territory as the demand increases. Many articles now generally sold in retail stores were first placed on the market by house-to-house solicitation. Cooking stoves, sewing machines, electric irons, and kitchen cabinets are examples.

House-to-house selling is a relatively expensive method of selling, although it may not be more expensive than selling similar goods through wholesalers and retailers. The salesman must receive a fairly high commission (often 30 to 60 per cent) because his sales volume is usually small. The manufacturer has the expense of recruiting, training, and supervising the salesmen, and delivering goods in small quantities. There is also a credit and collection problem in collecting from the salesmen or the consumers. Since the turnover of salesmen is usually high, new men must be constantly recruited and trained. The work is somewhat discouraging, especially if the salesmen must make cold calls, that is, visit prospects without appointments. New methods of securing interviews and new sales arguments are needed constantly to keep up the salesmen's enthusiasm.

Some sellers find that new men with little training will sell as many goods as experienced men because of their enthusiasm. When they lose their enthusiasm, sales decline and they quit. The large number of inexperienced and untrained men, however, has tended to bring the house-to-house salesmen into disrepute and make the work harder for experienced and competent men. Some producers selling through specialty men have

their best sales during business depressions for the reason that they can get more salesmen at such times.

Selling by mail and radio. Some sellers have no personal salesmen; they sell by advertising and deliver the goods by parcel post, express, or freight. Advertising may be carried in periodicals, over the radio, or by direct mail. Direct mail means that letters, catalogs, circulars, folders or other printed matter are used in soliciting business. Total sales of several well-known mail-order houses, and the hundreds of small specialty houses run into the hundreds of millions annually. Mail-order selling is important in reaching people in remote or sparsely settled sections where there are few stores. It is often used for goods unsuited to sale through retail stores. These may be perishable products, such as nursery stock (trees and shrubs), baby chicks; products with too thin a demand to warrant stocking by the retailers, such as scientific instruments or technical books; or luxury products with little demand in any one community. Perhaps the main reason for buying by mail is to obtain goods not available in local stores. Another important reason is that prices are sometimes lower than in the local stores. The large mail-order houses developed their business largely on the basis of low prices but this feature has been emphasized less in recent years.

Mail-order sellers are divided into (1) specialty and full-line houses and (2) sellers with one-time and repeat products. The specialty house handles only one or a very few articles. The full-line house carries many products and often issues a catalog. The specialty house must have a product of wide appeal or must select sales prospects with care, otherwise advertising costs will be too high to allow a profit. The full-line house offers many products; if a recipient of the advertising does not need one article he may need another. If he does not need a shirt, he may need shoes. If he does not need shoes he may need a new piece of furniture or perhaps some toilet articles. Consequently, the full-line house has more chances of securing an order from a single advertisement than has the specialty house.

The one-time product is a durable good which the consumer will not reorder for a long time, for example a stove or watch.

The repeat product is one that is soon used up and needs to be reordered; food and hosiery are examples. The full-line house selling many repeat goods appears to have the best chance to develop regular customers. Because the success of selling by mail often depends upon securing regular or repeat customers, mail-order sellers are very careful to adjust all complaints to the entire satisfaction of their customers.

Success in mail-order selling. Success in selling by mail or radio depends upon the number of orders received for each advertisement. In direct-mail selling it usually depends upon the percentage of sales from the mailing of a specific piece of advertising. The sellers mail out 1000 advertisements. A 1 per cent return means ten sales, a 2 per cent return means 20 sales, and so on. One seller may need a 3 per cent return to make a profit while another can make a profit with a 1 per cent return.

The cost of sending out a piece of direct-mail advertising may be from 3 to 30 cents; the average when mailed first-class is about 5 or 6 cents. A specialty house selling by direct mail should have an article selling from $3 to $40 and carrying a margin of 50 to 75 per cent to cover the cost of advertising, packing, and shipping. For example, consider two articles: A selling for $8 and B for $15, and an advertisement costing 6 cents. A costs the seller $4.50 and his cost of packing, shipping and overhead is 50 cents. B costs $8 and the packing, delivering, and overhead expenses are $1. For A there is a margin of $3 and for B a margin of $6 to cover advertising and profit. The success of the seller depends upon the effectiveness of his advertising as measured by the percentage of sales (returns).

On article A, the seller loses if returns are less than 2 per cent, breaks even with a 2 per cent return, and must secure more than a 2 per cent return to make a profit. On article B he breaks even with a 1 per cent return and makes a profit with any higher return. If he can receive more than 2 per cent return, he makes a very high profit. Suppose he sends out 1,000,000 pieces of advertising and gets a 2.5 per cent return; he will have sold 25,000 articles with a profit of $90,000.

The percentage of sales made from advertisements depends

TABLE 7–3
EXPENSES AND PROFITS OF A DIRECT-MAIL SELLER, PER 1000 ADVERTISEMENTS

	PERCENTAGE OF SALES				
	1.0	1.4	1.6	2.0	2.5
Article A, selling price $8					
Sales, number	10	14	16	20	25
Sales, dollars	$80	$112	$128	$160	$250
Margin ($3 per sale)	30	42	48	60	75
Advertising cost @ 6¢	60	60	60	60	60
Profit or loss	30L	18L	12L	0	15P
Article B, selling price $15					
Sales, number	10	14	16	20	25
Sales, dollars	$150	$210	$250	$300	$375
Margin ($6 per sale)	60	84	96	120	150
Advertising cost @ 6¢	60	60	60	60	60
Profit	0	24	36	60	90

upon the attractiveness of the article advertised, the price, the advertisement itself, whether or not a sample is enclosed, and the mailing list used. The article must be one that appeals to those receiving the advertisement and must be offered at an attractive price. The copy must be suited to the prospects; when a successful advertisement is developed, it may be used over and over again. The kind and color of paper used, the illustrations, the color of the envelope, and the postage, whether first- or third-class, are to be carefully considered. The time of the mailing, both the time of the year and the day of the week, may be important. The mailing list is of basic importance. Some people will buy by mail and many will not. Some will buy one article by mail and not another. The problem is to secure a list of those who will buy the seller's product by mail. His list of regular customers is perhaps his most valuable asset because he can circularize it over and over again. Mailing lists may be purchased for almost every conceivable type of prospect. Mail-order sellers often exchange lists. Securing a list suited to the particular seller and keeping it up to date is a constant problem. Once a good list is secured it may be used time after time.

The operation of a specialty mail-order seller has just been

described. Full-line houses may have a much higher percentage of sales returns because their catalogs offer many articles. Such houses may have advertising costs of from 5 to 15 per cent of sales. Total operating expenses of such houses have been reported by the Census as 25 per cent or less. This figure is lower than that of city department stores but higher than most rural stores. The expense of the large mail-order houses includes both wholesale and retail expense. Large mail-order houses have great buying power and manufacture some of their goods. Considering these facts it can be understood why they are often able to sell at attractive prices.

Questions

1. What are the methods which a manufacturer may use in disposing of his product?
2. What are the factors which influence a manufacturer's choice of outlets?
3. How does the fact that a manufacturer has a full line of products affect his choice of outlets?
4. What effect does consumer demand for a manufacturer's product have on his choice of outlets?
5. How is the manufacturer's choice of outlets influenced by (a) the territory covered? (b) his capital and sales ability?
6. Why do some manufacturers prefer to sell to a few large buyers? What are the disadvantages of such a policy?
7. What are the benefits to a manufacturer in developing consumer acceptance for his brand?
8. What are the advantages to the distributor in having his own brand? The disadvantages?
9. Can it generally be said that a manufacturer's branded product is superior to that of a distributor?
10. Can distributor's private brands be bought for less than manufacturers' nationally advertised brands?
11. Illustrate how the various stages of a manufacturer's development influence the outlets which he uses for his goods. When a change is made, give the reasons for the change.
12. What is a missionary salesman? Why are wholesalers sometimes opposed to the use of these salesmen by manufacturers?
13. What conclusions can be drawn as to the services of the wholesaler to the manufacturer?
14. What are the problems involved in the granting of exclusive agencies by manufacturers to wholesale merchants?

15. What are the advantages to a retailer of an exclusive agency? To the manufacturer?
16. Under what conditions is the policy of granting exclusive agencies desirable?
17. What provisions of a contract make an exclusive agency illegal?
18. What are the three methods which a manufacturer may use in selling direct to the consumer?
19. What are the problems involved in using door-to-door salesmen?
20. Upon what does success in selling by mail depend?
21. The National Biscuit Company manufactures a line of cookies, crackers, and other bakery products. It maintains a large number of distributing houses from which it operates trucks to supply its goods direct to the retail stores. What factors cause the National Biscuit Company to use this method of distributing its products?
22. Maryland tomato canners often employ sales agents who sell their entire outputs. Why is this sales method employed?
23. The large meat packers commonly operate branch houses from which they sell their meats to the retail butchers. Why?

B. Commodities

8

The Agricultural Marketing Problem

BECAUSE the farmer is an important political force, the marketing of his products is a subject of keen interest to Congress and the nation as a whole. This situation is not new. Only the more recent events will be considered in detail in this chapter, however.

The Basis of the Farm Marketing Problem

The fundamental change in the market. In the agricultural industry, as in manufacturing, the major development since colonial days has been the development of the farm plant from the household stage to the factory stage. In colonial days the primary objective of farm operations was to produce directly for the livelihood of the owner and his family and secondarily for the market. Gradually the purposes were reversed. Today the farmer's chief objective is to produce for the market; production for the direct needs of the owner and his family takes second place.

Frequently, the fact that agriculture, like manufacturing, has had revolutions is overlooked. Within a century after steam power was introduced into manufacturing it was adapted to agricultural equipment. Steam was followed by the widespread use of the gasoline engine on the farm. At the same time there was an improvement in farm tools and a development of more scientific planting, cultivating, and harvesting methods. The farmer, as the manufacturer, found himself generally in the position of offering his products in a buyer's market.

The decline in prices. During World War I, however, a seller's market existed. Prices skyrocketed and these high prices were accepted as normal. Following that war the prices of farm products declined precipitously.

The causes of this decline and the relatively low prices which continued to prevail were varied. Certain causes were external to the United States; among them were the following:

1. The armies of Europe were demobilized and many of the soldiers returned to farming, plowing the battlefields on which they had recently fought. Most of the countries of Europe are important producers of grain and livestock. With production resumed, Europe was no longer in need of American farm products.

2. Europeans were unable to buy American farm products although they desired to do so; Europe was bankrupt. Germany and France were fast spiraling to dizzy inflationary heights. Great Britain was seeking a loan or a gift. Europeans might have purchased American farm products with goods manufactured in Europe, but American industry and labor were opposed to this. The tariff effectively prevented the exchange of European manufactures for American farm goods.

3. European governments were adopting and following a policy of economic self-sufficiency. It was believed that a nation was stronger if it provided for the majority of its needs. Domestic agriculture was encouraged. This policy further diminished the demand for American farm products.

4. World War I greatly stimulated agriculture in Canada, Argentina, and Australia where land and labor were cheap. Modern agricultural machinery further reduced the cost of production. The American farmer could not compete against these low costs.

5. It was the policy of Great Britain to encourage by favorable legislation the Dominions to trade with the mother country. The wheat of Canada, Australia, and India was favored. The wool of New Zealand and Australia was preferred. Argentina was a market for British manufacturers and Argentine beef was favored at home.

Some of the causes for the price decline were internal, however:

1. During World War I the farm plant was overexpanded. The high prices received for farm products caused many acres to be cultivated which had previously never been farmed. These acres were slow to be withdrawn from cultivation. As a matter of fact it was only with great reluctance that the land was withdrawn from cultivation. Much of it had not been bought outright but had been purchased subject to a mortgage. Furthermore, the land had been purchased at inflated prices. As prices of farm products declined, a farmer had to increase his production in order to meet payments due on the mortgage. The production increases further depressed prices or at least prevented them from rising.

To illustrate the effect of farm financing at inflated land prices on the price of farm products let us assume that a farmer purchases 200 acres of land. The price of the land is $300 per acre and wheat is $2 per bushel. One half of the purchase price or $30,000 is borrowed at 6 per cent for 20 years. As long as the farmer can sell wheat for $2 per bushel, 900 bushels will pay the annual interest on his mortgage. When the price declines to $1 per bushel, 1800 bushels are required to pay the annual interest. To make his interest burden easier to bear, the farmer attempts to make his land more productive; at least, he will not withdraw it from production. If all farmers who are operating mortgaged farms increase their production, the price of farm products tends to decline further or does not rise.

2. The automobile truck and the tractor were substituted for horses and mules on farms and in the cities. In the decade 1920–29 the number of horses on farms declined about 30 per cent. In the cities the delivery wagon began to disappear. The replacement of horses and mules by trucks and tractors reduced the demand for grain and forage crops.

3. The farmer's constant interest in improving his production techniques has been aided by experimental stations and colleges of agriculture. Many of the improvements enabled the farmer to increase his production. In the face of a declining demand,

the greater volume produced caused his prices to decline. His farm, however, could still be profitable if his cost of production was also reduced.

4. The introduction of labor-saving devices throughout industry has taken place over a long period of time, but as it has occurred, it has helped to bring about a decline in the per capita consumption of foodstuffs. The decline in the consumption of grain was about 10 per cent and in meats it was about 10 per cent during the period 1910 to 1939.

5. The decline in the demand for food and clothing was also accentuated by changes in living and working conditions. Homes were better constructed and heated. Less energy was needed to resist cold. More people worked inside in heated factories or offices. Less clothing was needed. People rode to work in heated automobiles. The hours of labor were shortened.

Government Attempts to Improve the Market

Dissatisfied with the price situation, the agricultural industry turned to Congress for assistance, and a wide variety of plans evolved which were designed to elevate farm prices or provide for organizations and services that would facilitate the marketing of farm products.

Early attempts. The raising of prices by the limitation of production was not given much attention at first. The principal idea was to let the agricultural industry produce in such quantities as it saw fit and to sell the "surplus" abroad at whatever price was obtainable; the government paid the farmers for the difference between the domestic price and the foreign price. Little consideration was given to the effects which such a policy would have on agriculture in foreign countries or the retaliatory measures which might be taken against the United States. Bills providing for payments to farmers of sums which would equalize the difference between domestic prices and the price of the "surplus" sold abroad were fostered in the Senate by Mr. McNary and in the House by Mr. Haugen. In 1927 and 1928, McNary-Haugen bills were successfully steered through the

Senate and the House only to have the President exercise his veto power.

At the time the McNary-Haugen equalization fee plan was being considered, attention was also being given to the export-debenture plan. Essentially this plan provided that farmers were to be given a bounty on agricultural products exported. Congress failed to make the plan a law, however.

The next measure to be given attention was the domestic allotment plan. Farmers were to be given certificates which permitted them to sell part of their production in the domestic market, and the "surplus" above domestic consumption was to be sold in foreign markets at the prevailing price. This plan also failed to be enacted.

The Farm Board and its policies. On June 15, 1929, however, agricultural interests were successful in getting the Agricultural Marketing Act passed. This law provided for the establishment of a Federal Farm Board of eight members which was to administer the Act. The Board was authorized to take steps to prevent and control surpluses in any agricultural commodity. The Board also was authorized to encourage the organization of coöperative marketing associations and to make loans to coöperatives for the purpose of assisting in the more effective merchandising of agricultural commodities.

In August, 1929, the wheat market began to break and the Board authorized the formation of a central sales agency for the wheat coöperatives. Pending the formation of this agency the Board announced that it would grant loans of ten cents per bushel on unsold wheat, and 90 per cent of the value of wheat on which a price had been fixed by sale or hedging. By October, the price of wheat was dropping rapidly; on the 24th, wheat dropped ten cents per bushel. The Board then announced that it would make loans to coöperatives on wheat stored in the leading terminal markets and the decline in prices seemed to be halted.

The market continued to sag, however, and in February, 1930, the Grain Stabilization Corporation was organized which undertook to support the market by buying cash grain at market prices and May futures. This corporation and its affiliated co-

operatives were soon in control of about one half of the visible supply of wheat. Much of the corporation's holdings was sold in foreign markets. Domestic prices, however, continued to decline. The Board admitted that while something might have been done in the way of stabilizing prices that the outcome had not been all that had been expected.

From its experience of one year the Board concluded that in a major stabilization effort a large quantity of the commodity would have to be taken from the market in order to have any material effect on prices. Furthermore, the existence of a large accumulation of the commodity under any circumstances was bound to have a depressing effect on prices regardless of assurances that the accumulated supply would not be sold. The Board also realized that purchases in the cash market were inadequate to sustain prices; such purchases had the effect of throwing the cash market out of line with the futures market.[1] Once the purchasing for future delivery had been begun it could not be stopped since any cessation would interfere seriously with the hedging operations of elevators and processors. The storage problem was also a serious one. In price stabilization on a large scale storage space would, over a period of time, not only become scarce, but interfere with the ordinary movement of grain from production areas to processing plants.

The Board made a study of the world outlook for wheat and saw that the trends in acreage, production, and consumption in wheat-producing countries were such that wheat prices were likely to continue low. The Board could see no hope of preventing serious consequences to American farmers by coöperative marketing, stabilization measures, or plans to dispose of farm products in foreign markets. To the Board, the obvious remedy was curtailment of production and reduction of acreage. This measure was urged but little action followed.

The efforts to stabilize the price of cotton were similar both

[1] The cash market is the buying and selling of the actual commodity. The futures market is the buying and selling of contracts calling for the delivery of commodities in the future. A purchase of cash grain is hedged by the sale of a futures contract. A sale of a commodity in which grain is a raw material is hedged to the extent of the value of the grain by the purchase of a contract calling for the future delivery of the grain.

in method and results to those tried for wheat prices. Loans were offered and made to coöperatives but prices continued to decline; curtailment of production was recommended, but the recommendation was not generally followed.

The Board continued to make its stabilization purchases (probably with not a great deal of confidence in such action) and prices continued to decline. Acreage reduction was urged more vigorously and in 1931 cotton acreage was reduced about 10 per cent, but the Southern States increased their corn acreage 8 per cent and wheat acreage 13 per cent.

The Board recommended the adoption of a national land policy which would remove some lands from production or the possibility of being used for productive purposes, and thus restrict agricultural development. For example, it recommended sharp curtailment of appropriations for public irrigation and drainage projects as well as the repeal of the Homestead Act. The Board continued to encourage the development of coöperatives, but recognized that coöperative marketing in itself was not a solution for the market problem being faced. It also recognized that its policy of purchasing commodities to maintain prices encouraged farmers to continue production.

The situation of one branch of the Government trying to raise prices and restrict production did not appear logical to the Board when other branches were appealing for aid for the hungry and threadbare element of the population. Although the Board possessed no legal right to do so, it did dispose of part of its holdings for charitable purposes. Whatever the Board's opinion of the policy prescribed for it by law, the members were bound to adhere to the policy as closely as practicable.

The AAA. In accordance with the trends of the time a new administrative body was created in 1933 to deal with the agricultural situation in general and, specifically, with the marketing of farm products. On May 12, 1933, the President signed the bill which created the Agricultural Adjustment Administration. Powerful impetus to the program of the AAA was provided by the experience of the Federal Farm Board. It was the object of the AAA to establish the purchasing power of

farm commodities on a basis equivalent to their purchasing power during the period August, 1909, to July, 1914.

By the terms of the Act, the Secretary of Agriculture was empowered to enter into agreements with farmers to reduce the volume of production for market. As a consideration for entering these contracts, farmers were to receive certain "benefit" payments. The program was to be financed by a tax on the first processor of the commodity.

On January 6, 1936, the Supreme Court declared the processing tax and benefit payments to be unconstitutional and on February 29, 1936, the Soil Conservation and Domestic Allotment Act of 1935 was amended to provide for diversion payments to farmers who agreed to conserve their land by removing a part of it from the production of certain crops and engaging in soil-building activities. In 1937 the diversion payments averaged $81.93 per farmer.

On February 16, 1938, another Agricultural Adjustment Act was passed. The Act of 1938 continued the soil conservation program, the making of loans on agricultural commodities, and "parity" payments. Crop insurance for wheat was also provided. Production quotas were to be established by the Secretary of Agriculture but these quotas could be rejected if two thirds of the farmers voted not to accept them. One million dollars annually was appropriated to the Secretary of Commerce to be expended for the promotion and sale of farm commodities.

The plan of the AAA to adjust the supply of agricultural commodities to the demand was unfortunate in the drought years of the early thirties. The effects of the planned adjustments were small when compared with the damaging results of the drought. Feed shortages brought about such a curtailment in livestock that meat prices rose to a level that brought complaints from consumers.

Experience proved that the policy of buying large "surpluses" in order to improve the condition of the market was at best an unsatisfactory temporary policy and one to be avoided in the future. Experience also proved that a policy of exporting "surpluses" is limited by the competition of foreign countries.

When the policy of developing new products from agricultural commodities is considered, it is necessary to keep in mind the competitive situation which might be created if some product already exists to meet the need for which the new product is designed.

A policy of naming minimum prices below which no shipper could quote was also found unsatisfactory. The object was to secure higher prices for growers, but since the entire volume or the major portion of the volume of commodities which was shipped to markets could not be controlled, the Administration was forced to remark that "The mere establishment of minimum prices in the absence of effective volume regulation, however, is virtually as effective as pushing on a rope from the standpoint of increasing grower prices and returns."

The Coöperative Marketing of Agricultural Products

It has been one of the expressed objectives of the national agricultural marketing policy to foster the growth of coöperative associations for the distribution of farm products. Long before this was a part of the national policy, coöperative associations had made considerable progress among farmers producing all the major lines of agricultural commodities.

The greatest activity in the organizing associations occurred before 1920 but the number of associations did not reach its peak until 1930 when there were 12,000 active associations with approximately 3,100,000 members doing an annual business of about two and one-half billion dollars. The number of associations decreased to 7,400 in 1945 with slightly less than three million members. However, their business increased to $4,835,000,000, owing largely to high prices. There were also 2,750 farmers' coöperative purchasing associations doing a business of $810,000,000 in 1944.

Objects of coöperatives. The objectives of farmers' coöperatives are to reduce marketing costs; to increase demand; and to stabilize prices in order to increase the prices received by the farmers.

The coöperative association attempts to reduce marketing

costs by increased efficiency, by securing the profits of the private middlemen, and by reducing the duplication in marketing machinery. When efficiently managed, coöperatives often return worthwhile benefits to their members. If not efficiently managed, they are often able to pay no higher prices than competing private middlemen and are often forced out of business. Two coöperatives seldom compete at the same shipping point, which often means that the coöperative (elevator or creamery, for example) secures a larger volume of business than do the competing private shippers. The large volume may therefore enable it to operate at a lower unit cost. Unless it is less efficiently operated, it can secure for its members the profits of the private middlemen.

The local association assembles the farmers' products, ships them to central markets, and often grades and packs the products handled. The association in the central market receives goods from the country and sells them for the local associations.

The coöperative association often pools the farmers' products, by which is meant that all goods of the same quality received during a given period are handled as one lot. The same price is paid for all goods in a pool, although they may be sold at different times and prices. The farmer receives the average price realized on the sale of all the goods in the pool, less operating expenses. Many coöperative associations try to increase demand by advertising, by improving the quality of their products, and by having all markets supplied regularly.

Prices may be stabilized by keeping all markets regularly supplied. This is called *feeding the market.* Goods need to be distributed both at the right place and at the right time. The association tries to distribute goods so that all markets are evenly supplied. Goods should be so distributed that both gluts (over-supplies) and famines are avoided.

Early in the twentieth century the local associations realized the need for representation in the terminal markets and accordingly they established terminal sales agencies. They also organized regional marketing agencies. Attempts were made to organize nationwide sales agencies but those organizations which have been formed have been short-lived. On October

29, 1929, The Farmers National Grain Corporation was organized by the regional associations almost all of which turned over their marketing functions to the new national organization. The Farmers National opened bidding offices and operated elevators, but its operations, like those of its predecessors, were not successful and it ceased to operate at the close of the 1937–38 grain marketing season. The regional associations then began furnishing sales service for the local associations.

Grain coöperatives. The grain associations have been more numerous than associations handling any other kinds of farm products, but since 1930 they appear to have lost first position in volume of business handled to the dairy products associations. The peak for grain associations was reached in 1931 when there were 3,500 associations with about 705,000 members. By 1945 the number of associations had declined to 2,285 but membership was about 481,000. The amount of business in 1945, however, was $1,286,000,000.

Coöperative elevator associations in recent years have handled about one third of the grain moving to market, but only about one third of that amount—one ninth of all grain moving to market—has been handled by the regional marketing association. The Farmers National Grain Corporation handled but about 5 per cent of the grain moving to market.

Local associations have been none too strong financially; during the droughts of the 1930's they had difficulty in obtaining enough grain to pay operating expenses. In areas where grain farmers sell direct to feeders, some coöperatives have operated their own trucks to assist in making deliveries.

Dairy products coöperatives. In 1930, 2,458 coöperative associations were marketing dairy products. Their number had declined to 2,214 in 1945. Membership in these associations has shown a tendency to increase and the volume of business in 1944–45 was higher than ever before.

Coöperative creamery associations were well established by 1900. Like the local grain associations, they have developed regional coöperatives; the largest of these are:

Land O'Lakes Creamery, Inc., Minneapolis

Challenge Cream & Butter Association, Los Angeles

United Dairymen's Association, Seattle
Interstate Associated Creameries, Portland
Dairy and Poultry Coöperatives, Inc., Chicago
Midwest Producers Creameries, Inc., Indianapolis

In recent years these associations have manufactured and sold as much as one fifth of the total output of creamery butter.

Fluid milk marketing associations are a recent development. There were only 101 of these associations in 1930; but in 1934, 110 such associations handled about two fifths of the fluid milk sold in the United States. Three types of these associations have developed: (1) the bargaining association, (2) the associations which bargain and in addition process surplus milk, and (3) associations which perform all functions between the producer and the consumer. The activities of the straight bargaining association have been confined strictly to the negotiating of contracts and prices with dealers, and have resembled broker's functions. However, the tendency in recent years has been for milk associations to perform more of both manufacturing and marketing functions.

Livestock coöperatives. Coöperative livestock shipping associations were unimportant in 1900. In fact, only eight are known to have existed then. Twenty years later these associations numbered 1,416; in 1920 and 1921 they were being formed at the rate of one per day. In 1930 the number of livestock shipping associations was 2,153 with a membership of about 465,000. In 1944 these associations numbered only 642 but their membership was approximately 636,000. Their business volume declined during the recession years but in 1944 it was greater than ever before.

The decrease in the number of livestock associations has been due to a number of factors. Some associations were organized by enthusiastic but inexperienced coöperative leaders; the failure to obtain business volume and qualified management caused certain associations to fail. Some associations were consolidated with others. Improved truck transportation also brought its toll. In the 1920's, livestock producers were more dependent on railroads for shipping and the associations performed the service of arranging for cars, assembling carlots of animals,

and distributing returns. Motor trucks and improved highways, however, enabled livestock producers to deliver direct to the packer whenever convenient. Certain handling expenses were thereby eliminated, particularly charges for feeding, watering, and selling.

Like the grain associations, the livestock associations established coöperative sales agencies in the central markets. In 1942 there were 71 sales agencies which handled livestock valued at several hundred million dollars. The agencies developed facilities for the handling of livestock and made efforts to lower the cost of marketing. In 1930 the coöperative sales agencies in the central markets formed the National Livestock Marketing Association which organized two subsidiaries: the National Feeder & Finance Corporation and the National Livestock Publishing Association. The National Feeder & Finance Corporation then organized regional subsidiary credit corporations for the purpose of financing feeders.

Cotton coöperatives. In 1930 the number of coöperative cotton marketing associations was 261. That year the American Cotton Coöperative Association was organized to perform the functions of a national sales agency. It opened sales offices in all the important cotton-consuming markets and arranged for the financing of growers and the operating of an interior classing service through offices it established in the cotton-growing states. Members of cotton associations have consistently been required to sign contracts or marketing agreements. The number of associations reached 530 in 1945 and they had about 266,000 members, and did a business of $178,000,000.

Fruit and vegetable coöperatives. Fruit and vegetable coöperative associations are more numerous than cotton associations and they extend over a wider territory. Only a few of the larger associations have established their own sales agencies in the important consuming markets. In 1931, the National Fruit and Vegetable Exchange, Inc., was formed for the purpose of providing sales facilities on a national scale. In the marketing of citrus fruits the coöperatives have been relatively strong, especially in California where the majority of the crop is handled by them.

Tobacco coöperatives. The low prices following World War I caused tobacco growers to take more interest in coöperative groups. The Burley Tobacco Growers Association of Lexington, Kentucky, organized in 1921, boasted of a membership of 109,000 in 1926, but it discontinued operation that year. As prices improved, interest in coöperatives declined. In 1944 only 12 coöperatives with sales of $27,000,000 were reported. The early associations required their members to sign very strict contracts but the tendency has been to liberalize the terms of the agreements. In recent years, the tobacco contracts have contained a provision which permits the member to offer his tobacco for immediate sale, but if the bid is below the loan value set by the government the tobacco goes in a coöperative pool.

Conclusion on coöperatives. Coöperatives engaged in the marketing of perishables which must be moved rapidly from the point of production to a distant consumers' market have had the most successful results. Associations engaged in the storing and marketing of products and feeding the markets have shown less successful records. In recent years most of the coöperatives have increased their volume of business, but they handle a small proportion of the total crop volume.

The Commodity Exchanges

Our modern boards of trade or commodity exchanges dealing in agricultural commodities have developed as a result of attempts to handle the marketing of farm products in terminal markets. Although the idea of these exchanges extends at least back to the Middle Ages, those in America were organized chiefly in the expansion period following the Civil War. Today, facilities for organized trading in all the major commodities are available in the leading terminal markets.

The chief commodities in which futures trading has been conducted are wheat, corn, and cotton; the chief exchanges are the Chicago Board of Trade and the New York Cotton Exchange. In 1941 grain contracts composed about 60 per cent and cotton contracts about 22 per cent of the value of all futures

trading. A little more than 81 per cent of the physical volume of all grain trading was transacted on the Chicago Board of Trade. Over a period of several years the New York Cotton Exchange has accounted for about three fourths of the trading in cotton futures while the New Orleans Cotton Exchange has handled about one fourth and the Chicago Board of Trade approximately 1 per cent of the volume of trading. Deliveries on futures contracts customarily have been small, amounting to less than 1 per cent in the case of wheat, corn, and cotton.

Kinds of traders. Those who trade on the exchanges in relatively small amounts ordinarily have far outnumbered the traders in large amounts. The Commodity Exchange Administration found that on September 29, 1934, about half of the long accounts in wheat on the Chicago Board of Trade were for less than 5,000 bushels. The accounts on the short side of the market averaged 10,420 bushels.[2] An analysis of the occupations of the traders that day was also made.

TABLE 8–1

OCCUPATIONS OF FUTURES TRADERS ON CHICAGO BOARD OF TRADE

OCCUPATION	NUMBER OF TRADERS FOLLOWING THE OCCUPATION	OCCUPATION	NUMBER OF TRADERS FOLLOWING THE OCCUPATION
Farmers	2076	Unemployed	530
Grain companies and elevators	1820	Physicians	523
Commission houses	1085	Merchants	506
Housewives	1025	Millers	438
Retired, miscellaneous	793	All others	9997

Almost 600 occupations were represented among the 18,783 traders doing business that day. The number of traders and their varied occupations gives some indication of both public participation in trading on the exchange, and the inclination of certain groups to speculate.

[2] A long account is a trader who has bought a contract calling for the future delivery of a commodity. A short account is a trader who has sold a futures contract without having the commodity.

Although the size of the average account may be small, individual accounts have at times reached mammoth proportions. In 1937 one trader in September corn on the Chicago Board of Trade had a long position of approximately 7,000,000 bushels which was more than 80 per cent of the total long contracts then open in that future. A few weeks earlier he had been long more than 9,000,000 bushels of September corn, and simultaneously short about 10,000,000 bushels of December corn. The latter amounted to approximately 40 per cent of the contracts then open in December futures.

The movement of such large accounts in the market can have an effect on prices and the Commodity Exchange Administration has required a daily report on accounts involving more than 200,000 bushels of grain.

Regulation of commodity exchanges. From time to time, when prices of farm products have been low, political orators have seized on the opportunity to make political capital by charging that the boards of trade were responsible for the low prices although the organizations themselves had neither bought nor sold but had only provided facilities for those who wished to trade in a given commodity. It cannot be denied that members of the boards of trade have sometimes formed groups to sway prices one way or the other, but the corporations providing the trading facilities have refrained from trading in the commodities for which they have established an exchange.

The chief regulatory laws affecting boards of trades until 1936 were the Cotton Futures Act of 1915 and the Grain Futures Act of 1922. On June 15, 1936, the Commodity Exchange Act was passed. This Act, an amendment of the Grain Futures Act, provided for the regulation of trading in wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, and Irish potatoes. On June 30, 1936, the Secretary of Agriculture created the Commodity Exchange Administration to administer the Act.

By the terms of the Act, commission merchants and floor brokers were required to be licensed by the Secretary of Agriculture before they could conduct business on a market designated as a contract market (a market conforming to certain

requirements as prescribed by law). Money or securities put up as margin could no longer be commingled with the property of the commission merchant but were to be accounted for separately. The Commodity Exchange Commission, composed of the Secretary of Agriculture, the Secretary of Commerce, and the Attorney General, was given power to fix limitations upon the amount of speculative trading done by any person. Hedging transactions, however, were excepted from limitation. Fictitious sales such as "wash sales," "cross trades," or "accommodation trades" were prohibited. Also banned were "puts" and "calls," that is, options to buy or sell future contracts. For violations of certain sections of the Act a maximum penalty of a $10,000 fine and a year of imprisonment could be applied.

Questions

1. What fundamental change has occurred in the marketing of agricultural products since colonial days?
2. What conditions outside the United States caused low prices of farm products in the period following World War I?
3. What were the conditions or causes inside the United States which created low prices of farm products in the period following World War I?
4. Are the causes of the low prices of farm products following World War I operative today?
5. What early attempts were made to improve the price of farm products?
6. Why did the efforts of the Farm Board fail to improve the price of farm products?
7. What changes were made in the attempts to improve the market for farm products in 1933? In 1936? In 1938?
8. What are the objectives of farmers' coöperative associations?
9. Why did the number of coöperative marketing associations decline after 1930?
10. What are the three types of coöperative milk marketing associations?
11. Why did the number of livestock associations decline after 1930?
12. In what respects has the operation of coöperatives handling the various kinds of commodities been similar?
13. What types of associations have had the most success?
14. What conditions may promote the development of coöperative associations in the future?

15. What are the principal commodity exchanges?
16. What were principal provisions of the Commodity Exchange Act?
17. Coöperatives often attempt to increase the demand for their products. In recent years, the consumption of rayon and rubber as well as the following foods has increased: oranges, lettuce, carrots, sugar, spinach, canned fruits and vegetables. The consumption of kale, parsnips, and meats has been more or less stationary, while the consumption rate for wheat, potatoes, hay, and horses has declined. We can eat only a certain amount of food, and the wealthy man can eat no more than the workingman. What causes the demand for some products to increase? To decrease? To what extent can coöperative associations increase the demand for the products of their members?

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The Marketing of Grain

GRAIN MARKETING problems are concerned with getting the crop from farmer to the processor or feeder. The processors are millers, manufacturers of cereal, feed and starch, distillers, and maltsters. Considerable grain is fed to livestock on the farm where it is cultivated or is sold to neighboring farmers for feed.

Grain markets may be classified into country markets and terminal markets, although certain markets possess the characteristics of both. In the country markets, located in small towns throughout the grain belt, grain is bought and sold in relatively small lots. Some is assembled into larger lots and shipped to terminal markets where it is bought by processors or grain merchants. The chief terminal markets are in Minneapolis, Kansas City, and Chicago.

The Country Marketing of Grains

Organization of the country market. The groups which operate in the country grain markets are:

1. Elevator operators
2. Interior brokers
3. Feeders
4. Truckers
5. Mill buyers
6. Buyers for terminal grain merchants.

There are three kinds of country elevators—coöperative, in-

dependent, and line. Coöperative elevators may also be either independent or line since some farmers' coöperative associations operate a number of elevators. Line elevators, the most numerous of the three types, are directed from a central office. The independent elevators are individual enterprises neither owned by line companies nor operated by coöperative associations.

Although the interior brokers negotiate purchases of grain for anyone who may desire it, they seldom contact the grower directly. Most of the grain that they purchase is owned by a country grain elevator.

Throughout the grain belt, stock feeding is carried on in conjunction with grain farming. The larger feeders, however, do not produce enough grain to meet their needs. They buy the necessary additional grain direct from farmers who do little or no stock feeding or they buy the grain after these farmers have sold it to local elevators.

Individuals who possess trucks suitable for hauling grain buy direct from farmers, haul the grain to what appears to be the most favorable market, and sell it. Truckers' purchases, however, are a small fraction of the total grain crop.

Various types of grain processors of one kind maintain warehouses and factories in the grain belt. They buy grain from elevators and farmers and store it until such time as they need it for manufacturing into finished products.

Sometimes employees of grain merchants in the terminal markets visit rural areas and make purchases of grain from farmers and elevators. A very small amount, however, is bought directly from farmers.

Operators of country elevators. The operation of a country grain elevator may include the following functions:

Buying	Loading out	Conditioning	Grinding
Weighing	Obtaining cars	Mixing	Shipping
Receiving	Storing	Financing	Insuring
Elevating	Grading	Drying	Selling

Country elevators often handle a variety of commodities in addition to grain, for example: prepared feeds, seeds, fertilizer,

fencing, coal, lumber, and farm implements. In handling such merchandise they perform the usual functions of a retailer.

A line company operates a number of elevators. Their facilities are found chiefly near railroads in the central and northwestern grain-growing regions. Hundreds of these country elevators are either owned or leased by elevator companies which have their main offices in the terminal markets. Formerly, the most important owners were the railroad companies which served the grain producing territory. This relationship between the railroads and the terminal elevator companies dates from the passage of the Hepburn Amendment (1906) to the Interstate Commerce Act of 1887. After the passage of this amendment the railroad companies could no longer operate elevators. Where new railroad lines were being extended into the grain producing area there was keen competition for the grain traffic. A railroad company, to assure itself of traffic, built elevators and leased them to operators of terminal grain markets. These leases were made on terms very advantageous to the terminal grain companies. Where this relationship existed, the warehouse companies outbid independent buyers in the country to the extent that the local buyer almost disappeared and left the farmer with the narrowest range of choice as to the place or price at which he might market his grain.

The purchase of grain by country elevators. Country elevators buy grain from farmers on the basis of "to arrive" bids which they have received from firms in the terminal markets. These bids are subject to the regulations of the grain exchanges where the bids originate. Bids are frequently made after trading has ceased on the exchanges and usually they must be accepted before the exchange opens the following day. An elevator operator, on the basis of his "to arrive" bids, may telephone farmers in his locality and buy their grain. The grain is loaded into cars and shipped to buyer in the terminal market within the "to arrive" time specified in the bid. In other cases elevator operators buy on the basis of their knowledge of current prices and the grade of the grain.

The grade or quality is an important consideration in determining the price paid by the elevator operator to the farmer.

To determine the grade of a farmer's grain the elevator operator examines it for shrunken kernels, admixture of other grains, dirt, smut, heating, moisture, insects, and tests it for weight. He then decides the grade which he will assign to it.

The grain standards in use in this country are established by authority granted to the Secretary of Agriculture by the United States Grain Standards Act, passed August 11, 1916. The various grades of grain are described in the *Handbook of Official Grain Standards of the United States.* These standards must be used in connection with grain which moves in interstate commerce. The Act also provides that grain may be shipped without inspection and grading by a Federal inspector at the point of shipment to or through a point where such an inspector is located. Consequently, Federal inspection and grading are seldom conducted at country points. Grain purchased at country markets is inspected and graded with more or less accuracy, depending on the efficiency of the operator of the elevator and his inspection process. The equipment used in the inspection process is not likely to be as modern and efficient as that used by inspectors in the terminal markets.

The elevator operator's knowledge of what price to offer the farmer for a particular grade of grain may be obtained from many sources: radio, telephone, telegraph, mail and newspapers all serve to convey the needed information. Price cards and circular letters sent out by commission houses also furnish information concerning grain prices. "Price currents," cards or letters containing more information than price cards, are another medium. The elevator operator may have received "on track" or "to arrive" bids from terminal grain dealers. These bids specify the prices which the terminal grain dealer will pay for a given kind and grade of grain. The central offices of some line elevator companies mail or wire price quotations and instructions for their local managers to follow in making purchases. This information may be supplemented by telephone when necessary. Other line companies instruct their managers to follow a given "price current." With price information from the Chicago or other markets, the elevator operator is able to quote a price on whatever grade of grain may be offered to him.

With current price information from the Chicago or other markets and a knowledge of the grade of grain before him, the elevator operator offers a price to the farmer. In arriving at the price offered, the elevator operator located in the territory tributory to Chicago may deduct from the quoted price for a given grade in Chicago, the cost of freight to Chicago, the cost of handling grain through the elevator, and the desired profit per bushel. For instance, if No. 2 red wheat is quoted at $1.70 in Chicago and the cost of freight is five cents, elevator expenses average three cents, and the desired profit per bushel is two cents, the price quoted to the farmer would be $1.60.

The exact price paid to a farmer is often influenced by the amount of competition among the buyers operating in the local market. Since the various buyers, in a given country station will pay the same freight, the competition centers around the expenses of elevator operation and the net profit desired or expected. The expenses of elevator operation vary with the efficiency, size, and type of organization.

The difference between what the country elevator operator pays a farmer for a given grade of grain and the price that grade of grain may be selling for in the terminal market fluctuates because demand conditions and supply conditions do not remain the same at all times. The degree of competition may cause the spread between country market and the terminal market prices to be greater or smaller. When the competition is intense, country elevators may not be able to earn their operating expenses because of the higher prices they must pay farmers for the grain.

In the past some grain has been purchased prior to harvest from farmers on the basis of a contract made between the elevator operator and the farmer. These contracts have specified the kind of grain to be delivered, the grade, the price, and the time of delivery. However, the arrangement has not been satisfactory to the farmer when his grain has failed to meet the grade specified in the contract or if, at harvest time, the grain is selling at a price higher than that specified in the contract. Consequently, it has been found desirable to purchase the grain on the basis of the market prices prevailing at the time of

delivery and to determine the grade and dockage at that time. Arrangements have also been made to ship to the terminal market a farmer's grain separately and remit the sale proceeds (less a certain commission to the elevator) to the farmer. In this way the grain could be graded by impartial and skilled inspectors in the terminal market, but the arrangement does not appear to be a general practice.

At times grain has been purchased from farmers on the basis of a sample submitted. Whether or not the sample was representative has been open to doubt; the farmer may have been unskilled in taking representative samples. At other times the elevator operator may have visited farms and bought grain in a bin or a crib as a round lot, with very little reference to the grade.

The sale of grain by country elevators. Grain bought by country elevators may be resold in the local market, sold "on track" or "to arrive" in the terminal market, or it may be consigned to a commission firm. If the grain is consigned, a notice of shipment and bill of lading is forwarded, perhaps with a draft attached. If the grain is consigned to a firm in Chicago, the cars are opened upon arrival and a sample taken by the Grain Inspection Division of the Department of Agriculture of the State of Illinois. The sample is identified with a ticket showing (1) the car number, origin, and location in the railroad yards; (2) the railroad over which it traveled; (3) car contents; and (4) the consignee. The sample is then sent to the State Grain Grading Office where it is graded in conformance with both Federal and Illinois requirements. Early next morning a small sample labeled with the grade is delivered to the consignee.

From the samples the commission man offers the grain for sale to prospective buyers who may be terminal elevator operators, millers, feed manufacturers or other processors, shippers or exporters. A prospective buyer views the samples and when he believes that the grain is offered at the right price a purchase is consummated. The seller makes a note on the sales side of his trading card of the car number, the grain, the price, the buyer, and the terms of delivery. The buyer makes a similar

notation on the purchase side of his trading card. Later the buyer's and seller's trading cards are sent to their respective offices and confirmations of the trade are exchanged. The seller also sends the shipper a confirmation of the sale. The seller prepares a disposition order instructing the railroad agent to deliver the car according to the buyer's instructions. After this order is endorsed by the railroad agent, it is returned to the seller for endorsement and then forwarded to the purchaser. Certificates of inspection are also requested from the Grain Inspection Division.

An official weight certificate is obtained which serves as the basis for making an invoice that covers details of the transaction. The invoice is forwarded to the purchaser and after payment has been made an "account sales" is prepared for the shipper. The account sales shows all expenses incurred in connection with the shipment and sale of the grain as well as the net proceeds of the transaction. To the account sales are attached a check for the net proceeds, plus all supporting documents such as duplicates of the weight and inspection certificates and the freight bill. All are then forwarded to the shipper.

Some country elevators hedge their purchases and sales of grain. The object of hedging is to protect the country elevator against price declines which might wipe out its merchandising profit or result in a greater loss. Hedging will be discussed after the operations of the grain exchanges have been explained.

Terminal Grain Market Organization

The organizations and individuals operating in the terminal grain markets are:

1. Terminal grain merchants
2. Processors
3. Exporters
4. Commission merchants
5. Brokers
6. Speculators.

Some terminal grain merchants operate nationally and internationally. They have elevators throughout the United States

and in Canada and may own the barges and boats that move their grain from producing areas to consuming areas. They conduct both domestic and export transactions and are members of the principal grain exchanges.

Terminal grain companies operate in three major marketing capacities. They operate as merchant middlemen, as agent middlemen, and as public warehousemen. In the last-mentioned capacity they are functional middlemen specializing in the performance of the storage function. They provide the physical facilities for protecting grain against a variety of hazards and for holding the grain until they desire to move it along the channels of trade.

As merchant middlemen (or grain merchants or dealers) the terminal grain companies take title to grain. They are the largest grain merchants or merchandisers in the terminal markets. Like any merchant, they intend to resell what they have bought at a price higher than they paid for it and thus earn a merchandising profit. Terminal companies also operate as commission merchants. In this capacity they do not take title to the grain but act as an agent for country shippers or others.

A large amount of grain is moved to the terminal markets. In these markets the various processors can obtain the quality and quantity of grain needed for their finished products. The latter cover a wide range of items. Among them are flour, starch, corn meal, oatmeal, mixed feeds, glucose, prepared breakfast foods, malt, beer, and whiskey.

Some of these products are designed for sections of the processors' respective markets which differ as to quality preferred or as to the consumer product that is manufactured from them. As a result, the various processors search for different kinds and qualities of grain, especially in large markets where there is a possibility of finding the particular quality and quantity desired. They either locate in the terminal markets or send representatives to them.

A few exporters operate in the terminal markets of seaport cities. They buy grain f.o.b. some designated point or free on board ship and sell it c.i.f. That is, they agree to deliver grain at a foreign port and pay costs of handling at the port, insurance

and freight. The major portion of the export business in grain is done by terminal merchants themselves, however.

Commission merchants are located in all terminal markets. The terminal merchants who buy and sell on their own account also do business on a commission basis. Commission merchants who deal in grain perform the following services:

1. Receive grain
2. Negotiate sales of grain
3. Furnish market information
4. Finance country elevators
5. Procure or assist in procuring cars for the shipment of grain
6. Negotiate purchases and sales of contracts calling for the future delivery of grain.

A small number of brokers also negotiate sales and purchases of grain in the terminal markets. The brokering of grain is done by firms that also operate as commission merchants.

Speculators in contracts calling for the future delivery of grain seldom handle grain physically. Their primary business is assuming the risks of price declines and of advances through selling and buying contracts that call for the future delivery of grain. Through the facilities of the exchanges anyone may become a speculator. Few, however, can speculate in a professional manner and all may incur losses at one time or another. Because proximity to the market is highly important, many speculators are located in the terminal markets.

Anyone who buys grain or any other commodity assumes the risk of a decline in price. In this sense every merchant, whether he handles grain or other products, is a speculator.

The Grain Exchanges

The organization and operation of the exchanges. The buyers and sellers of grain in the terminal markets have formed corporations which provide the facilities for trading. These corporations do not buy and sell grain. Their function is to provide a place where buyers and sellers of grain can meet to conduct business. One large room in the exchange building is designated as the exchange hall. The hall is equipped with

modern communication facilities over which information is received from and sent to other grain exchanges and elsewhere.

The three principal grain exchanges in this country are the Chicago Board of Trade, the Minneapolis Chamber of Commerce, and the Kansas City Board of Trade. Although the Minneapolis exchange bears the title "Chamber of Commerce" it is not a chamber of commerce in the usual sense of that term. The Chicago Board of Trade is the largest of all grain exchanges and does about 80 per cent of the total volume of futures trading in grain in this country. The principal foreign grain exchanges are those located in Liverpool, Winnipeg, and Buenos Aires.

A set of rules and regulations governs the trading of the members of the exchange. One of these rules provides that only members may trade in the exchange hall. Anyone else desiring to trade on the exchange must do so through a member of the exchange. In order to become a member it is necessary to secure approval of the membership committee and to buy a membership from the Exchange (if there is a vacancy), or from someone who wishes to sell his membership. The purchase price varies with business conditions. At times memberships have sold for a few hundred dollars; at other times they have sold for several thousand dollars.

Exchange members trade in "spot grain," that is, they buy and sell the actual commodity for immediate delivery. They also trade in contracts calling for the future delivery of grain. Such contracts, termed "futures," are bought and sold according to the month in which the buyer desires delivery and in which the seller desires to make delivery. The seller has the option of delivering the grain on any business day of the month for which he is obligated to deliver. Trading is most active in grain contracts specifying delivery of grain in July, September, December and May.

The unit of trading—so many bushels of a particular grain—is prescribed by the exchanges. On the Chicago Board of Trade 5,000 bushels is the unit of trading. However, trading may be conducted in lots which are multiples of 1,000 bushels.

Futures contracts are usually not fulfilled by actual delivery of the grain. Instead, contracts are offset in much the same way that banks offset checks in a bank clearing house. For instance, one who sells a contract calling for the future delivery of grain may buy a contract. The purchased contract is set off in the Board of Trade Clearing House against the one which was sold. The trader then is relieved of his obligation to deliver spot grain.

Futures contracts cannot be bought or sold without making a deposit on the contrast. This deposit is called "margin." The minimum margin required is specified in the exchange rules. More than this minimum may be required.

If the margin required for wheat is 20 cents per bushel and a futures contract for 5,000 bushels is either bought or sold, $1,000 must be deposited with the broker negotiating the purchase or sale. If a contract calling for the delivery of wheat is bought at $1.90 per bushel and the market price of the contract declines to $1.85, the purchaser's margin has been impaired to the extent of 5 cents per bushel or $250.00. He has lost $250 since the contract he bought is now worth $9,250 instead of $9,500. His broker will ask him to restore the margin to the original $1,000 by depositing a check with the broker for $250. If the purchaser of the contract orders a contract sold to offset the one he purchased, and thus withdraws from the market, the broker will return what is left of the margin minus the commission for the transaction. If the commission amounts to $15, the amount returned in this case would be $735.00.

Since grain can be or may be delivered on a futures contract, the prices of spot grain and futures contracts are very closely connected. Conditions affecting the price of spot grain influence the price of contracts calling for the future delivery of grain and vice versa. This relationship is clearly indicated by the practice of bidding or offering a price for spot grain at a discount from, or a premium above, the price of contracts for a given month.

The price of futures contracts fluctuates continually because so many conditions have an effect on the demand for and supply of grain. A trader who believes that the price of grain will decline and is selling futures contracts is called a *bear*. A trader

who believes that the price of grain will increase and is buying contracts is called a *bull.* When the general trend of grain prices is downward, the market is described as *bearish.* When the general trend is upward, the market is *bullish.*

One who sells a contract and does not have a warehouse receipt indicating that he has grain equal to the amount specified in the contract is called a *short.* One who buys a contract is a *long.* In other words, a bear is a short and a bull is a long.

Hedging against fluctuations in the price of grain. Grain merchants and processors of grain can use the facilities of the exchange to protect themselves against adverse fluctuations in the price of grain. The object is to provide some assurance of earning a small profit although by not hedging they might earn a larger profit.

Hedging may involve the offsetting of a purchase of cash grain with the sale of a futures contract and the later offsetting of the sale of the cash grain by the purchase of a futures contract. When a country elevator buys grain in the local market which is to be hedged, the elevator operator instructs his commission firm in the terminal market to sell a futures contract. Later, when the grain is shipped and sold, the commission firm is ordered (by standing or specific instruction) to close the hedge, that is, to buy a futures contract.

The transactions can be illustrated as follows:

An order to buy or sell a contract calling for the future acceptance or delivery of grain may originate in a branch office or in the main office of an exchange member. The order to sell 5,000 bushels of December wheat may be given in a branch office with the limitation that the sale is to be made at a certain price and by a certain time or it may be understood that the sale is to be made immediately at the prevailing price. At the time the selling order is given a margin is deposited by the seller in the branch office. The order is transmitted by private wire to the Chicago office where a telegraph operator transcribes it to a form marked "private wire." It is given an order number, stamped by a timeclock, and given to a telephone operator who transmits it to another telephone operator on the Exchange floor. The

Exchange floor operator signals the order to the firm's pit broker who secures the attention of a buyer, gets agreement on the price, signals the execution of the order back to the telephone operator on the floor and thus to the main office of the firm. Here the price is noted on the order which is again stamped by the time-clock and then passed to a sending telegrapher to report back to the branch office. Such is the method of handling "flash orders."

If the order is not a flash order, the telephone operator on the floor of the Exchange will rewrite the order and send it to the pit broker who, after negotiating the sale, sends it back with a notation of the sale price. Original orders may, in some instances, be conveyed directly to the pit broker.

The price paid by the country elevator to the farmer for grain is usually below the price of the grain in the terminal market. The latter price must cover the cost of freight to the terminal market, the cost of handling the grain by the country elevator, and the net profit desired by or allowed to the elevator. If the price of No. 2 red winter wheat is $1.60 per bushel in Chicago and the freight to Chicago is 10 cents, elevator expenses or cost of handling is 6 cents, and the desired profit is 4 cents, the price which will be paid in the local market will be $1.40 per bushel. If the country elevator makes a purchase of 5,000 bushels of wheat from a farmer on this basis on June 18, for instance, he will wire his commission merchant to sell 5,000 bushels December wheat. This sale will be executed in the wheat pit at the prevailing price of December futures contracts which may be $1.65. The grain purchased from the farmer is not delivered in fulfillment of this contract. Several days later, the elevator will consign the 5,000 bushels of wheat to his commission merchant and on June 28 it may be sold at $1.55, the cash or spot price having dropped five cents during the ten-day interval. The commission merchant has been instructed to close the hedge when he sells the cash grain. This he may do by negotiating the purchase of 5,000 bushels of December wheat at the prevailing market price which has dropped to $1.61.

A summary of the above transactions by the country elevator follows:

PURCHASES		SALES	
June 18—5,000 bushels wheat @ $1.40......	$7,000	June 18—5,000 bushels Dec. @ $1.65........	$8,250
June 28—5,000 bushels Dec. @ $1.61........	8,050	June 28—5,000 bushels wheat @ $1.55......	7,750
Total...........	$15,050	Total...........	$16,000

Sales....................................	$16,000
Purchases................................	15,050
Gross margin.............................	$ 950
Elevator expenses and freight (5,000 bushels @ 16¢)...	800
Net profit...............................	$ 150

In this illustration the elevator earned but 3 cents per bushel ($150 on 5,000 bushels) because the decline in the spot price (from $1.55 to $1.50) was 5 cents while the decline in the futures price (from $1.65 to $1.61) was 4 cents, resulting in the reduction of the net profit by one cent per bushel or $50. Instead of obtaining 20 cents per bushel gross margin on the grain the elevator obtained the difference between the $1.40 and $1.55 or 15 cents. If the elevator had not hedged, there would have been a loss of one cent per bushel since freight and elevator expenses amounted to 16 cents, or one cent more than the gross margin. This one-cent loss was prevented, however, by the sale of a December contract at $1.65 and the later purchase of a December contract at $1.61. This was a gain of 4 cents per bushel on the futures transaction which, added to the 15-cent gross margin on the cash grain, made a total gross margin of 19 cents. Subtracting the expenses and freight of 16 cents leaves a net profit of 3 cents per bushel or $150 on 5,000 bushels.

One object of the terminal grain companies is to earn a profit plus the cost of carrying grain until it may be delivered on the futures contracts which are sold at the time the grain is purchased. If the price of futures contracts at the time the grain is purchased does not exceed the price of grain by the amount which it costs to carry grain until delivery, it may appear that these carrying charges would not be earned. This assumption, however, is not necessarily true. By the time the grain must be delivered on contracts cash grain is very likely to be selling at

such a premium over the futures that at least the carrying charges can be earned. This follows from the fact that whoever has grain to deliver on a contract must obtain a warehouse receipt from a regular warehouse; he cannot obtain such a receipt unless he is willing to pay the cost of carrying the grain from about harvest time until he is required to make delivery.

The foregoing can be made more concrete by using prices which prevailed at given times. On November 30, 1942 a quantity of wheat was bought at $1.38¼ per bushel, or at a premium of 8⅜ cents over the price of May contracts. The purchase could have been hedged by the sale of a May contract at $1.30⅜, but the transaction would not permit the earning of the carrying charges if the wheat were delivered on the contract. If it were delivered, the result would be a loss of 8⅜ cents per bushel plus the cost of carrying the wheat until May. Such a result should be avoided. On May 5, 1943 this wheat might have been sold at $1.64¾ and the hedge closed at $1.46¼ when the wheat was at a premium of 18¾ cents over the contract. There was a gross margin of 26 cents per bushel on the grain but a loss of 15⅞ cents per bushel on the contracts. The result was a gain of 10⅛ cents per bushel or 1.947 cents per bushel for each month the grain was carried. This gain should be in excess of the cost to the terminal operating company of carrying the grain.

A summary of the above transactions is as follows:

PURCHASES		SALES	
Nov. 30 wheat @......	$1.38¾	Nov. 30 May contract @...	$1.30⅜
May 5 May contract @.	1.46¼	May 5 wheat @..........	1.64¾

Total sales........................	$2.95⅛
Total purchases....................	2.85
Gain......................	$ .10⅛

A terminal company which operates warehouses need not hedge its purchases of grain as indicated above. When the management deems it advisable to buy grain and take the risk of earning grain storage costs and a profit it may do so. This decision will be made when it is judged that the price of grain is going to advance faster than the accumulating carrying charges.

In the above illustration, the advance of cash grain in about

five months was 26 cents, which is without question much in excess of the cost of carrying the grain. If the company management had judged this to be the course which cash grain prices would follow in the five months after November, the purchase of the grain would not have been hedged. A gain of 26 cents would have been made instead of a $10\frac{1}{8}$ cents gain.

The delivery of grain on futures contracts. The delivery of grain on a futures contract can be made only by acquiring a warehouse receipt issued by a warehouse that has been declared regular by the board of directors of the exchange. A seller who is to deliver the grain furnishes the exchange clearing house with a signed notice of delivery in which the warehouse receipt to be delivered is described. The clearing house gives this notice to a buyer who then presents it at the seller's office. The buyer pays for the grain and the seller delivers the warehouse receipt to the buyer.

If the buyer wishes to obtain the grain described in the receipt he returns the receipt to the State Registrar for cancellation. The canceled receipt is then taken to the office of the public elevator operator who issued it and cars or boats are ordered to the elevator to receive the grain. The grain is loaded into cars or boats, inspected by the State Grain Inspector, and a grade assigned.

All grain in terminal warehouses which is "delivered" on futures contracts is owned by the warehousemen. Usually this grain is not actually delivered on futures contracts. In a twenty-year period ending in 1943 not one per cent of the total grain contracts traded on the Chicago Board of Trade was fulfilled by actual delivery of grain.

The Chicago Board of Trade, like all other exchanges which provide for futures trading, selects for regular delivery on futures contracts certain recognized grades and varieties of grain. The grades and varieties deliverable at contract price are known as contract grades. Other grades and varieties are made deliverable at a premium above or a discount below the contract price. In 1943 there were eight kinds of No. 1 and four kinds of No. 2 wheat which could be delivered on wheat contracts.

With so many possibilities for delivery on a futures contract,

the buyer is uncertain as to what kind and grade of grain he will receive. However, he may be fairly sure that he will receive the grade and kind of grain which is most advantageous for the seller to dispose of at the time of delivery. Buyers of futures contracts have often been dissatisfied with this situation and have urged that measures be taken to provide more assurance as to what will be delivered on contracts. This uncertainty in futures contracts, however, is the very essence of their attractiveness to the seller. If the grades of grain which the seller could deliver were reduced, there would be more uncertainty as to the possibility of the seller obtaining a particular grade for delivery. Since the risk to the seller thus would be greater and price fluctuations would probably be wider, futures contracts would become less attractive. This would tend to reduce the volume of futures trading and the possibilities of hedging.

Questions

1. What organizations operate in country grain markets?
2. What are the three kinds of country elevators?
3. What does the business of a country elevator involve?
4. What interest do railroads have in grain elevators? Can they operate elevators? Why would they lease them on favorable terms to terminal grain companies?
5. What is meant by buying grain on a "to arrive" basis?
6. Where does a country elevator obtain information as to what prices to pay farmers for grain?
7. How does a country elevator operator arrive at the price he pays a farmer for grain?
8. Does the difference between the price of grain in the country grain markets and in terminal grain markets remain the same? Why?
9. How does a country elevator sell grain?
10. Describe how grain is handled by a commission merchant in a terminal grain market.
11. What organizations operate in terminal grain markets?
12. How do terminal grain companies operate?
13. Why do processors want different qualities of grain?
14. What services do commission merchants perform?
15. What is a grain exchange? Does it buy grain in its corporate capacity?
16. What are the three principal grain exchanges in this country? Outside this country?

17. Which is the largest grain exchange?
18. Can anyone trade in the exchange hall?
19. What is meant by "spot grain"?
20. In what grain contracts is trading most active? Why?
21. What is the unit of trading in grain on the Chicago Board of Trade?
22. Are futures contracts usually fulfilled by actual delivery of the grain? If not, how are they fulfilled?
23. What is meant by margin? Why is it required?
24. Why are the price of spot grain and the price of futures contracts very closely connected?
25. Define the following terms: bear, bull, short, long, contract grade.
26. On July 14 a country elevator buys 5,000 bushels of No. 2 red wheat from a farmer. Spot wheat is selling at $1.50 per bushel and September contracts are selling at $1.55 per bushel. Freight to Chicago is 5 cents per bushel and all other elevator expenses including commissions, average 3 cents per bushel. The desired profit is 2 cents per bushel. On July 28 the wheat is shipped to Chicago and sold. In the meantime the spot market has dropped 3 cents and the futures market has dropped 2 cents.

    Set up a table of purchases and sales indicating which are spot transactions and which are futures transactions. What was the profit or loss on the entire transaction?

10

The Marketing of Cotton

THE PROBLEMS in marketing cotton are those of getting cotton from planter to processor, or from farm to textile mill. Cotton, like grain, first must be assembled in country markets and then moved to central markets. Buyers and sellers of cotton also have formed commodity exchanges where they trade both in the spot commodity and in futures contracts.

The Country Marketing of Cotton

The country buyers of cotton. The cotton farmer sells most of his crop in nearby markets. The buyers to whom he may sell are:

1. The local store
2. Local cotton buyers
3. Ginners
4. Resident or traveling buyers for cotton shippers or merchants
5. Mill buyers
6. Local coöperative association.

Since the earliest days of cotton planting the proprietor of the local general store has functioned as a cotton buyer. The primary reason why the local storekeeper is an important buyer is that it is uneconomical for the textile mills to buy the many small crops direct from countless growers scattered across the southern half of the United States. The proprietor of the local

store assembles the small crops of the cotton farmers in his area into lots which can be economically handled by the larger buyers, especially the textile mills.

Another reason is based on the small farmer's need for credit. This need for credit also has existed since the earliest days of cotton planting. Often the small farmer obtains most of his food and other supplies needed between crops from the local store on credit. The proprietor of the store requires a settlement when the farmer's chief money crop, cotton, is harvested. The settlement is made by applying the value of the cotton against the debt owed to the store. In periods when the price of cotton has been low the farmer has been continually in debt to the local store.

The local buyers of cotton purchase small lots during the harvesting season. They operate with little capital and buy direct from the farmers, or from the local store, or wherever they may obtain a supply on which a small profit can be made.

Ginners purchase cotton on their own accounts either before or after cleaning the cotton. Some buy on a commission basis for others.

The cotton of the larger growers may be bought by a resident or traveling buyer for a cotton shipper or merchant. They obtain their supplies chiefly from other local buyers.

Buyers for southern textile mills sometimes buy cotton which is raised near the factory and also visit throughout the producing area to buy from the large-scale producers. In general, however, this is not an economical buying method for the mills because the grade and quantity seldom meet the mills' requirements.

Coöperative cotton marketing associations buy cotton direct from farmers and any saving which is made in the cost of marketing is returned to members in the form of a patronage dividend. The proportion of the total crop handled by these associations varies from year to year but it probably averages about 10 per cent. It is estimated that in 1944 there were 533 of these associations with about 258,000 members.

Financing the cotton farmer. The cotton farmer's need of credit and his financing by the local store proprietor has already been mentioned. During the nineteenth century cotton factors

did much of this financing. They made loans to farmers on the basis of a mortgage secured by the growing crop or the crop to be planted and the farmer agreed to consign his cotton to the factor for sale. However, as local banks developed they financed the grower to a larger extent and the cotton factor's role in financing growers declined in importance. In recent years, organizations formed or sponsored by the Federal Government have made loans to cotton farmers.

Buying cotton in country markets. The cotton buyer in the country market purchases cotton by three different methods: bale buying, hog-round buying, and basis middling buying.

In individual bale buying, the buyer examines a sample from each bale and offers a price for each bale in accordance with its quality. This method is used in buying very small lots.

In hog-round buying, the buyer examines samples from each bale and offers what he determines to be a fair average price for the entire lot. This method and the basis middling method are used to purchase larger lots.

In basis middling buying, the buyer quotes a basic price for middling seven-eighths inch cotton. The bales are classed (graded) later. For grades better than middling and for staples longer than seven-eighths a premium over the basic price is paid. For grades poorer than middling and for staples shorter than seven-eighths a discount from the basic price is paid.

The country buyer of cotton examines samples and judges its color and lustre, the nature and amount of foreign material it contains, the length and character of the fiber or staple, and how it has been ginned or prepared. Cotton standards are established by the Department of Agriculture by authority of the United States Cotton Standard Act passed March 4, 1923. The regulations issued under this Act recognize three botanical types: sea-island, American-Egyptian, and upland. Practically all cotton now raised in the United States is the upland variety. For upland cotton thirty-seven different grades and twenty different staple lengths are recognized. These standards must be used for cotton which moves in interstate commerce but the Act provides that cotton may be bought on the basis of a private type or by actual sample.

A large proportion of local dealers do not classify cotton as accurately as it is done by other buyers. They lack both the skill and the equipment necessary for accurate classification.

The local buyer's knowledge of what price to offer the farmer for his cotton is obtained from many sources: radio, telephone, telegraph, teletype, mail, and newspapers. Prices are quoted in cents and hundredths of a cent per pound. A hundredth of a cent is called a point and price fluctuations are expressed in points.

The price paid for spot cotton and the price of contracts calling for the future delivery of cotton are very closely connected. In general, anything which has an effect on cash cotton prices will influence future prices and anything which affects future prices will influence cash prices. Evidence of this interrelationship is the practice of quoting prices as so many "points off" or "points on" the price of contracts that specify delivery of cotton in a given month.

With a knowledge of the current selling price for a given class of cotton and a knowledge of the class of cotton being offered, the local buyer quotes a price to the farmer. In arriving at the price, the local buyer deducts the cost of freight to the market, his costs of handling the cotton, and his desired profit from the price quoted by the nearest port, mill, or interior central market. The exact price paid to the farmer is often determined by competitive bidding among the buyers who are operating in the local market.

The sale of cotton by country buyers. The store, small local buyer, and ginner sell the largest portion of the cotton which they buy to cotton shippers or merchants. The shipper or his representative after coming to an agreement on the price acquires from the seller a gin, compress, or warehouse receipt indicating the weight of the cotton, its class, and the bale markings. Payment is made by check.

A buyer for a cotton shipper, however, may pay for the cotton with a sight draft. The seller endorses the draft and deposits it in his bank along with the bill of lading and the proper receipt. These documents are forwarded to the shipper's bank, or to a correspondent bank of the country bank; when the draft is hon-

ored or payment is made, the documents are forwarded to the shipper.

When local buyers are of the opinion that the price of cotton is going to rise, they may not be willing to sell their cotton at current prices but they will agree to sell it "on call." This means that the buyer agrees to pay the seller so many hundredths of a cent (points) on or off (above or below) the price of futures contracts calling for delivery in a given month. The seller, as an inducement to sell immediately, is given the right to name the time when he wishes to fix the price, that is, complete the transaction. The latest date on which the seller can fix the price is usually set two or three days in advance of the date when notice of delivery on the future contract must be given.

Central Market Organization

Cotton moves from the smaller towns or country markets of the South to larger towns or central markets. Each of these larger markets assembles cotton from several smaller markets and also serves as a country market for the cotton raised in the territory adjacent to the town. Illustrative of these central markets are such widely separated cities as Savannah, Georgia and Dallas, Texas.

The principal individuals and organizations which operate in these markets are:

1. Shippers, 2. brokers, and 3. factors.

The shipper is a general cotton merchant who may operate in both domestic and foreign markets or confine his attention to one of them. The leading shippers have representatives in all principal markets. In some of these markets they are represented by branch houses which buy, sell, or do both. The largest cotton shipper is Anderson, Clayton & Co. In the ten years from 1925 to 1935 this company handled from 10.6 per cent to 17.5 per cent of the total cotton raised in the United States.

Spot brokers sell cotton on commission for country buyers and for holders in central markets. In Memphis the term "f.o.b. men" is applied to spot brokers. The cotton is sold from samples although the cotton which these samples represent is in some

country market loaded in cars, or waiting to be loaded. When loaded it is "free on board," that is, ready for shipment to whatever point the buyer directs. Brokers who buy for foreign customers on terms that include the cost of the cotton plus insurance and freight to the foreign destination are known as c.i.f. brokers.

Factors receive cotton from independent country buyers on consignment. The owner notifies the factor that a certain amount of cotton is being shipped over a certain route and may furnish selling instructions. If notice of the shipment is not received from the owner before the arrival of the cotton, the factor's first notice may be the railroad manifest. This document describes the shipment and indicates its origin. Samples are taken and the lot either placed on sale or held until instructions are received from the owner. With the decline of financing by factors, their business declined and they turned to the outright purchase of cotton, thus becoming cotton merchants or shippers.

Textile mill buying offices are located in some of the central markets and these are called mill markets. In these markets, cotton owners and representatives of cotton owners call at the mill offices and offer cotton.

The Cotton Exchanges

In the principal central markets of the South cotton traders have formed exchanges. The members of these exchanges buy and sell spot cotton among themselves and buy and sell futures contracts on the principal futures exchanges. The principal cotton exchanges are the New York Cotton Exchange and the New Orleans Cotton Exchange. In 1943 the New York Exchange did about 70 per cent of the total volume of futures trading in cotton. About 30 per cent of the total volume was done on the New Orleans Exchange and less than 1 per cent was done on the Chicago Board of Trade.

The organization and operation of the cotton exchanges. The cotton exchanges are very similar in organization and operation to the grain exchanges. Their points of similarity may be summarized as follows:

1. The exchange corporations do not trade in cotton but pro-

vide facilities for members to trade in cotton and cotton contracts.

2. Only members may trade in the exchange hall.

3. A set of rules and regulations governs trading on the exchange.

4. Delivery on futures contracts is at the seller's option. As in the case of grain, he may deliver on any day of the month and with the proper adjustment deliver one of several classes of cotton.

5. Contracts are usually not fulfilled by actual delivery of cotton but they are offset in a clearing house.

6. Contracts cannot be bought or sold without depositing a margin.

7. The prices of contracts and the prices of spot cotton are closely connected because contracts are convertible into cotton.

Hedging against fluctuations in the price of cotton. Large scale buyers and spinners make use of the exchange facilities to hedge against price fluctuations. Buyers of small amounts, because of the small amounts which they handle or because of their failure to understand hedging, however, usually do not use the facilities of the exchanges to protect themselves against price fluctuations.

The price in the country market at which a cotton merchant buys cotton normally will be below the price in the nearest central market by the cost of the freight plus the merchant's costs of handling and a small profit. Spot prices in the central markets are frequently below futures prices by the cost of carrying cotton to the time of delivery on the contract. Consequently, the price in the country market can be quoted as so many points off the price of futures contracts.

If a cotton shipper's average expenses are 27 points per pound and the freight cost to the central market is 75 points, the shipper, if he desires a profit of 10 points per pound, will pay the seller 112 points below the price in the central market. If the price in the central market is 22.16 cents per pound, the price in the country market will be 21.04 cents per pound.

The price of cotton futures contracts is likely to be above the central market price by the cost of carrying cotton from the date of sale until the time of delivery on the futures contract. It must

be emphasized that this is not always true because demand and supply conditions vary both with time and place. It makes little difference to the cotton hedger whether the price of futures contracts is above or below the price of spot cotton. The important thing is the relationship between spot and futures prices. There are some fluctuations in this relationship but it tends to remain constant.

If the price in the central market is 22.16 on October 6 and the cost of carrying cotton until July is 15 points per month, the price of December contracts can be assumed to be 23.66. In any given instance the relationship may not be a difference of exactly 150 points but this is a tendency.

A cotton shipper who paid an average of 21.04 cents per pound for 100,000 pounds of cotton in the country market could hedge this purchase by the sale of a July contract at 23.66 cents. This cotton may be held until January 22 when it is sold to a cloth manufacturer at 19.76 cents, the price of spot cotton having declined 240 points from the central market price on October 6. The price of July contracts normally would decline by about the same amount. The decline is not necessarily by the same amount, however; it may be more or less than 240 points. When the cotton is sold to the cloth manufacturer this sale is hedged by the purchase of a July contract. This purchase may be made at 21.01 cents per pound, when the price of futures contracts has declined 265 points. A summary of these transactions follows:

PURCHASES		SALES	
Oct. 6—100,000 lbs. cotton @ 21.04.....	$21,040.00	Oct. 6—100,000 lbs. July futures @ 23.66	$23,660.00
Jan. 22—100,000 lbs. July futures @ 21.01.............	21,010.00	Jan. 22—100,000 lbs. cotton @ 19.76....	19,760.00
		Total sales..........	43,420.00
	$42,050.00	Total purchases......	42,050.00
		Gross profit.......	$ 1,370.00
		Expenses, freight, and cost of carrying for 3½ months, 100,000 lbs. @ 1.545 cents per lb............	$ 1,545.00
		Net loss.........	$- 175.00

If the purchase of this cotton had not been hedged, the loss—c.i.f. expenses as well as the loss of 128 points on spot cotton—would have been $2,825. That is, the expenses, freight, cost of carrying plus a loss of 128 points on the spot cotton would have been lost.

The cloth manufacturer may also hedge his purchase of cotton from the cotton merchant. He may have obtained an order for 352,000 yards of cotton cloth from a chain store at 19 cents per yard. He has based his price to the chain store on July contracts which were selling at about 23.66 cents per pound, labor costs of 27.12 cents per pound, manufacturing, administrative, and selling expenses of 20 cents per pound, and a profit of 2 cents per pound for the finished cloth. He knows from experience that 100,000 pounds of raw cotton will produce about 88,000 pounds of finished cloth or 352,000 yards.

The chain store does not want the cloth delivered until March. The manufacturer's transactions occurred the same day as those of the cotton merchant but they were not necessarily dealing with each other. On October 6 when the order for the cloth was taken a July future for 100,000 pounds was bought at 23.66 cents per pound. On January 22, the cloth manufacturer bought cotton at 19.76 cents per pound and began to manufacture the cloth. At the same time he sold a July future to hedge his purchase of cotton. A summary of these transactions follows:

PURCHASES		SALES	
Oct. 6—100,000 lbs. July futures @ 23.66.	$23,660.00	Oct. 6—352,000 yds. cloth @ 19.0......	$66,880.00
Jan. 22—100,000 lbs. cotton @ 19.76.....	19,760.00	Jan. 22—100,000 lbs. July futures @ 21.01	21,010.00
	$43,420.00		$87,890.00

Total sales..		$87,890.00
Total purchases..........................	$43,420.00	
Labor cost (88,000 lbs. @ 27.12 cents per lb.)..	23,865.60	67,285.60
Gross profit....................................		$20,604.40
Manufacturing, administrative and selling expenses (88,000 lbs. @ 20 cents per lb.)..		$17,600.00
Net profit....................................		$ 3,004.40

The delivery of cotton on futures contracts. The delivery of cotton on a futures contract is very similar to the delivery of

grain on a futures contract. As in the case of grain, the amount actually delivered is usually less than one per cent of the total volume of trading, and the contracts are offset through the clearing house.

Actual delivery of cotton may be made, however, by a member of the exchange who has sold a contract and thus is obligated to deliver. This is done by a member of the clearing house who prepares and delivers to that body a transferable notice that he will make delivery according to his contract five days after the date of the notice. The clearing house then passes the notice to an Exchange member who is obligated to receive cotton, namely, to the member who has bought a contract and who has not offset it by the sale of a contract. The member to whom the notice is passed may sell a contract thereby relieving himself of the obligation to accept delivery, or he may take delivery of the cotton. If he desires delivery, he notifies the one originally issuing the notice and requests the warehouse receipts which are described in the notice.

The actual delivery of cotton on futures contracts differs from the delivery of grain on futures contracts in regard to the place of delivery. Grain must usually be in warehouses located in the same city as the exchange. In the case of cotton, a contract sold on the New York Cotton Exchange may be fulfilled by delivery in New York or in seven southern cities. Chicago and New Orleans contracts can be fulfilled by delivery in Houston and Galveston. Furthermore, one or numerous grades and qualities of cotton may be delivered on a contract at price differentials for quality. These possibilities make the acceptance of delivery undesirable.

Cotton, like grain, can be delivered only by the passing of a warehouse receipt for cotton stored in a warehouse licensed by the exchange. Also, as in the case of grain, it has been alleged that there is a considerable concentration of control of public warehouses for the storage of cotton.

Significance of Futures Trading

The significance of futures trading is that the price of futures contracts is related directly to the price of spot commodities.

The basis of this relationship is the convertibility of one into the other. A futures contract may be sold and the commodity delivered on the contract or a futures contract may be bought and the commodity received on the contract. The consequence is that any manipulation of the price of futures contracts has an effect on the price of the spot commodity and any manipulation of the price of the spot commodity has an effect on the price of futures contracts.

Although the volume of trading in 1943 was not unusual, the value of cotton and grain contracts traded is estimated to be ten billion dollars. The significance of futures trading, however, cannot be appreciated by considering only statistics. Futures trading is understood by a few and misunderstood by many. People who have had but the slightest comprehension of the processes have engaged in it. On the other hand, it has been engaged in by those who comprehended it and who have benefited accordingly.

Since there have been national markets for farm products, farmers have followed the course of cotton and grain prices as reflected by the prices of futures contracts. Frequently the farmer's attitude toward futures trading has been one of suspicion, a suspicion that has sometimes been justified. Investigations and news reports during the past seventy-five years have frequently provided unquestionable facts that the price of grain was being manipulated. These reports have served to intensify his suspicions and he has turned to Congress and the State legislatures for correction of the conditions which made manipulation possible.

Intermittently people of a wide range of occupations avail themselves of the facilities of the exchanges to trade in futures. Their knowledge of grain and cotton and the futures contract is superficial to say the least. Many inspired by an avarice born of limited financial means, have ordered their brokers to buy or sell contracts for them when they had but the slightest knowledge of the risk they were undertaking. Only when their trading has run its course has the full realization of the magnitude of the risks which they have undertaken become evident. With losses considerable they have returned to their vocations—wiser,

perhaps, and frequently with an antagonistic attitude toward the exchange.

The futures contract was not devised so that the public might give vent to its whims and speculative impulses. It was devised in order that the marketing risks could be shifted to persons familiar with the risks involved and financially able to assume them. It was not devised so that one trader could obtain an advantage over another although that may be the result. The futures contract was designed to provide processors and merchants with some assurance that they would earn the usual profits of their undertakings. When conditions arise so that these normal functions of futures trading are circumvented, it is the duty of the State so to regulate exchange transactions that the designs of those who would create abnormal market conditions are thwarted.

Questions

1. To whom may the cotton farmer sell his cotton?
2. Why has the general store been important in the handling of cotton?
3. Why have factors declined in importance in the financing of the cotton farmer?
4. What are the three different methods of buying cotton?
5. Where does the country buyer obtain knowledge of what to pay a farmer for his cotton?
6. Why is the price of spot cotton and futures cotton very closely connected?
7. How does the country buyer arrive at the price he pays the farmer for cotton?
8. To whom may country buyers sell cotton?
9. What is meant by selling cotton "on call"?
10. What organizations operate in central cotton markets?
11. Describe how factors handle cotton.
12. Name the most important cotton exchanges.
13. How are cotton exchanges similar to grain exchanges?
14. How does the actual delivery of cotton on futures contracts differ from the actual delivery of grain on futures contracts? How is it similar?
15. What is the significance of futures trading?
16. On December 10 a cloth manufacturer obtains an order from a men's shirt manufacturer for 176,000 yards of cloth at 26 cents

per yard. He has based his price to the shirt manufacturer on May contracts which were selling at 21.78 cents per pound, labor costs of 42.25 cents per pound, manufacturing, administrative, and selling expenses of 33 cents per pound, and a profit of 6 cents per pound for the finished cloth. He usually needs 50,000 pounds of raw cotton to produce 44,000 pounds (176,000 yards) of cloth. The shirt manufacturer wants delivery of the cloth in April.

The cloth manufacturer hedged his sale of cloth on December 10 when May contracts were selling at 21.78 cents. On February 27 the cloth manufacturer bought the necessary cotton at 24.32 cents per pound and began to manufacture the cloth. At the same time, he sold a May contract at 25.84 cents per pound to hedge his purchase of cotton.

Set up a table of purchases and sales indicating which are futures and which are spot transactions. What was the net profit or loss on the transactions?

11

The Marketing of Industrial Goods

To PRODUCE goods for consumption either by the industrial consumer or the household consumer four broad classes of goods are required: equipment, supplies, parts, and raw materials. Each of these kinds of goods has it own set of marketing problems. In this chapter some of these problems will be discussed.

Classification of Industrial Goods

Equipment is called capital goods, that is, goods used to produce other goods such as machinery, factory buildings and the like. Included in this class of goods are lathes, drill presses, punch presses, milling machines, stamping machines, grinding machines and a wide range of metal-cutting machinery. Also included in this class are spindles, looms, furnaces, pumps, sewing machines, conveyors, locomotives, trucks, and other kinds of machinery that perform a variety of tasks.

Some equipment is built to special order to meet the needs of the buyer. Since it is built to the specification prescribed by the customer, there may be only one of its kind manufactured. Other kinds of equipment are highly standardized and may be used and manufactured in large lots, for example, lift trucks, typewriters, boilers, desks, motor trucks, and adding machines.

The unit price of industrial equipment is frequently high. Certain items cost the buyer more than one hundred thousand dollars while others sell at much lower prices.

Supplies are goods which are consumed by the industrial user in carrying out some of his major functions. Examples are lubricating oil, coal, gasoline, crude oil, polishing compounds, cleaning compounds, files, typewriter ribbons, and paper. Some industrial consumers purchase these supplies in relatively large lots while others buy them in small quantities. This affects the method of distributing them.

Parts are formed, fabricated, assembled, or otherwise processed units of some finished product. Examples are tires, electric motors, batteries, radio tubes, special stampings and castings, and any element of a finished product. Whether or not the manufacturer should make or buy a given part is often debated. A manufacturer who specializes in the production of a certain part may be able to produce it at a lower cost than can the manufacturer of the finished product.

Raw materials vary widely in source and character; among them are lumber, ore, grain, cotton, livestock, chemicals, rubber, wool, and petroleum. It is these that are bought so that equipment, supplies, and parts may be used to produce a finished product. The sources and production of raw materials are sometimes controlled by the manufacturer or processor. The problems of uncertain supplies and of buying the raw materials are thus avoided.

The foregoing classification of industrial goods is not absolute. What may be a raw material for one manufacturer is properly considered the supply item for another; or a supply item of one manufacturer may be an equipment item for another. The gradations between the different classes of industrial products cannot be drawn with exactness nor to fit all conditions. In a study of the general problems in the marketing of industrial products an exact classification is not necessary.

The Market for Industrial Goods

The industrial market is composed of a wide range of business organizations, governmental organizations, and farmers. Business organizations constitute the largest portion of the industrial market. Among these are manufacturers, wholesalers, retailers,

transportation companies, construction companies, public utility companies, lumber companies, mining companies, and a wide variety of service establishments. The governmental organizations range from village governments to the Federal government and its divisions and bureaus. Farming is an industry which consumes large quantities of products some of which are manufactured specifically for that industry, for example, agricultural implements and mixed feeds.

The demand from all these organizations for industrial products is derived from or based on a demand for goods and services which are consumed by the household consumer. This demand is affected directly and indirectly by a wide variety of factors.

Selling Industrial Goods

The methods and problems of selling industrial goods vary somewhat with the kind of industrial goods. There is a certain basic similarity, however.

Equipment. The demand for equipment has an effect on the methods and problems of selling it. As just indicated, the demand for equipment is a derived demand. For example, the industrial demand for packaging machinery is derived from consumer demand for the packaged products. The machinery manufacturer and his salesmen should thoroughly understand this consumer demand.

Based as it is on the demand for consumer goods, it avails little to lower the price of equipment in times when the demand for consumer goods is weak. Firms with old equipment are inclined to continue to operate with it and firms with new equipment feel no need to replace it. In times of rising demand for consumer goods the demand for industrial equipment increases.

Manufacturing processes and parts of processes do not remain static. There is a continuous search for more economical methods of production. When old methods of production are discarded, the use of a particular manufacturer's equipment may be abandoned; consequently, he must give attention constantly to the development of new models or new equipment. A machine manufacturer may develop a type or model which makes

others in the same category obsolete, thus causing other manufacturers of the machine to experience a sales decline.

A manufacturer's equipment designed to be used in the manufacture of a given kind of product may experience a decline in sales because the use of the product declines, or may increase as a result of increased sales of the product. For example, a greater use of plastics will tend to reduce the demand for metal-cutting machinery and to increase the demand for plastic-molding equipment.

The importation of consumer goods tends to reduce the demand for industrial equipment produced in this country. Textiles produced abroad and consumed in this country cause the demand for textile machinery to be lower than it would be otherwise. When the demand for consumer goods tends to increase, the manufacturer of equipment may soon notice a decline in his sales.

The outlets for equipment depend upon the nature of the equipment and the quantities used. Highly specialized machines built to the order of the customer are sold direct to the user. Standardized equipment which can be sold in large quantities is also sold direct. Some standardized equipment which is bought in small amounts by the user is sold to industrial distributors who resell it to retailers or to industrial users.

The manufacturer's agent and the selling agent are also used advantageously to distribute equipment. By using these agents, the manufacturer pays for a sales force only as it makes sales. The use of manufacturer's agents provides a sales force in selected markets while the use of a selling agent shifts all selling problems to a specialist organization.

The type of salesman needed to sell equipment also depends upon the nature of the equipment. Highly specialized equipment requires a salesman with considerable technical knowledge. Men who are both good salesmen and good technical men or engineers are difficult to find. To overcome these difficulties, the manufacturer may employ salesmen who are not expert engineers and provide the services of engineers when professional engineering advice is needed.

Important purchases of industrial equipment are not usually

made in the same manner as raw materials and supplies. Purchasing agents usually exercise considerable authority in the purchase of supplies and raw materials. In the case of equipment, however, the purchasing authority is frequently vested in a committee composed of major executives of the firm. The technique of selling such a committee does not differ from that required to influence the decision of any committee but it is frequently time-consuming. Furthermore, the interval of time between sales may be long and irregular. The consequence is that salesmen who sell equipment of large unit value are paid both a salary and a commission.

Because of the relatively large unit price of some equipment it may be difficult for small firms to pay cash. In some instances, the equipment manufacturer then sells on an installment basis or may accept in full or partial payment for the equipment stocks or bonds issued by the firm.

Equipment manufacturers who have patent monopolies may solve the difficulty of securing large cash payments from buyers by leasing the equipment to the user rather than selling it outright. The lessee of the equipment agrees to pay the manufacturer so much per unit of product turned out by the machinery. The equipment manufacturer determines when new machines will be installed. It is not necessary that salesmen be continually on the alert to discover when new equipment should be purchased by the user.

Raw materials. The sale of two important raw materials, cotton and grain, has already been discussed, pages 143-172. Much iron ore is obtained from lands owned by the steel companies or from lands under long term lease to the steel companies. When these companies mine their own, no selling problem is involved.

What is considered to be a raw material by some firms, however, is a processed material to others as, for example, cloth, flour, lumber, pig iron, copper, lead, aluminum and a variety of processed forms of steel such as billets, bars, rounds, wire, sheets, angles, channels and others. These materials often are passed to another unit of the same firm which considers them to be raw materials. The unit further processes the goods; wire is

woven into fencing, for example, and rolls of steel are converted into box straps.

A firm which controls commodities from the raw material to the finished goods is an integrated concern. An integrated organization does not face the selling problems which a non-integrated organization must meet. Successive sales organizations are eliminated, pricing problems are avoided, and the product of one stage of manufacture does not encounter sales resistance from the next stage of manufacture or distribution.

The non-integrated manufacturer of a product for either industrial or household consumption must contend with a wide range of selling problems. Among these are advertising, pricing, and the obtaining, training and maintaining of a sales organization.

Parts. A part is a manufactured unit which is complete in itself but is used as an element of another product and is thus consumed. Examples are the parts for automobiles, refrigerators, radios, washing machines, and other household appliances. Examples for industrial equipment are motors, gears, tool holders, springs, shafts, bearings, conveyor buckets or plates, and motor guards and housings.

The two markets for parts are the original equipment market and the replacement market. The original equipment market consists of manufacturers who do not manufacture all the parts or sub-assemblies used in their finished product. The majority of automobile manufacturers buy tires instead of making them. Washing machine companies purchase electric motors. How far to proceed in the direction of purchasing parts rather than producing them is often a difficult question.

The needed parts or sub-assemblies are sold direct from the parts manufacturer to the manufacturer of the assembled product. The number of purchasers may be small but the quantities sold are large; credit is sound, and the demand fairly stable and continuous. The services of a wholesaler are not necessary.

The replacement market is composed of the consumers of the completely assembled product. The user of the assembled product needs only one or a small number of parts at a given time. The demand may be fairly continuous and in its aggre-

gate rather large but it is spread as wide as are the users. Replacement parts are therefore sold to industrial distributors, hardware, electrical, and automobile accessory wholesalers, repairmen, chain stores, and other retailers.

Supplies. Any industrial consumer will use a small amount of certain supply items and a large amount of others. When the items are consumed in large quantities, they can be sold direct to the user. If the quantity consumed is small, the items can be distributed economically through wholesalers and retailers.

Buying Industrial Goods

The buying of the various kinds of industrial goods involves problems which are peculiar to the kind of goods. Some of these problems will now be discussed.

Equipment. Engineering and production executives usually have considerable influence in determining what specific kind of equipment will be purchased. Since these executives are responsible for the volume of output, quality, and cost of the finished product, they usually have the authority for selecting the equipment which will permit them to accomplish their objectives.

It is important for the salesman of industrial equipment to determine which firm member makes the final decision when equipment is to be bought. This member is not always readily recognized. The executive who gives the final okay to a purchase of equipment may do so only on the recommendation of another executive whose work is more closely related to the use of the equipment. The general manager, president, chairman of a committee, or the purchasing agent may voice the final assent to a purchase but the actual decision was made by engineers.

Factors to be considered in buying industrial equipment. The final decision as to what to purchase represents a compromise of the several factors that should be considered.

Frequently, but not always, the initial cost of equipment is the primary factor. Equipment which is used directly in proc-

essing has a direct effect on the cost of the finished product. A piece of equipment with a high initial cost can result in a lower unit cost per finished product, if the life of the equipment is long and its output high.

A second factor to consider is the operating cost of the equipment. Among these costs of operation are the labor required, the fuel consumed (if any), rate of depreciation, interest on the investment, repairs, and obsolescence. These costs should be calculated on the basis of the unit of output if the equipment is direct production equipment.

The trade-in or scrap value of the equipment must also be considered. Whatever this value may be, it necessarily has an effect on the ultimate cost of the equipment. If this value is low and the equipment is processing machinery, the cost per unit of output will be higher.

Ease of operation is also a factor. If a piece of equipment can be operated easily the operator is less fatigued. A tired operator is a costly operator. Furthermore, there is a tendency to use more women operators. Equipment which is easy to operate is more suitable for women employees.

When there is any choice in the matter, equipment which involves considerable risk in its operation should not be purchased. Equipment which involves risk in its operation has a fatiguing effect on the operator and, if accidents occur, a demoralizing effect on other workers. Accidents not only interrupt production but also affect a firm's liability insurance rates.

Efficiency of operation is another factor to be considered. To be efficient, a piece of production equipment should operate continuously and at high speed. Automatic machinery may have a strong appeal for several reasons, but it can be expensive equipment if its operation is frequently interrupted due to improper functioning or the breaking of some part.

The service required from the vendor may also have an influence on the type of equipment purchased. If specialized servicing of the equipment is required, either the vendor or the purchaser must be prepared to do it. If the vendor services the equipment, this cost must be included in the initial price of the equipment or a special agreement must be made to cover main-

tenance costs. Inquiry should be made concerning the vendor's organization and reputation for rendering the service.

Finally, an important factor to be considered is the terms upon which the equipment can be purchased. If the purchaser is short of funds or desires to use his funds in other capacities, some method of financing the equipment must be devised. The purchaser should study the financing cost because it has an effect on the ultimate cost of the equipment. If the vendors will accept the common or preferred stock of the purchasing corporations, they should consider carefully the risks involved.

The salesman of industrial equipment who can present his product adequately in terms of the foregoing factors is prepared to sell. This means, however, that he must be about as familiar with competing equipment as he is with that produced by his company. The purchaser who makes his decision only after an adequate investigation of the equipment in terms of these same factors will buy the right equipment.

Raw materials. The specific kind of raw materials needed is also determined by production or engineering executives, or by both, since they are responsible for the volume, quality, and cost of production. After these executives have determined the specifications which the raw materials are to meet, they may have nothing further to do with purchasing until the specifications are altered.

In setting up the specifications for raw materials, consideration is given to the quality required in the finished product, the quantity and price of the raw materials to be purchased, and the place of purchase. Responsibility, however, for the purchase of the right quality, at the right time, in the right quantity and at the right place is assigned to the purchasing department.

A fundamental policy of any organization is that adopted in regard to quality of the finished product. When the consumer becomes aware of the quality of a given product, he will notice any marked variations from this quality and he may notice minor variations. Consequently, it is important that the purchasing department obtain the kind and grade of raw materials which will maintain the quality of the finished product. The

purchasing department also must take steps to insure that the quality of the raw material delivered meets the specification on the purchase order. Visual inspection alone is rarely adequate. Laboratory methods should be used, not that the vendor will attempt to deliver materials which fail to meet specification but because various and sundry errors can and do occur.

The quantity of a raw material to be purchased at any given time depends on several conditions or factors. The first of these is the volume of output planned for a certain production period. If the volume to be produced in a given period will consume 100,000 tons of steel, that much steel must be on hand. If it is not available, delivery dates of the finished product are affected and the firm's reputation is injured.

Finished products are usually composed of a variety of raw materials, for example textiles, steel, copper, paint, and rubber. On the basis of weight or other physical unit a standardized finished product will contain these materials in fixed proportions. Although subject to qualifying factors, the raw materials must, in general, be purchased in quantities proportionate to the amount used in the finished product.

The present and probable future price of a given raw material have a bearing on the quantity which may be purchased. Prices of some raw materials are sensitive and subject to sudden changes. The ideal, which is rarely accomplished, is to buy when the price is at the bottom of one of its dips; to buy substantially before the price rises, and cautiously as it declines. Although difficult to achieve, skilled buyers do so with considerable efficiency.

The amount of reserve stock necessary to meet production emergencies also affects the quantity of a raw material which should be purchased. Although production budgets can be established with considerable accuracy, consumer demand is capricious. Demands for fashion merchandise may change without advance notice and orders pour in for an article for which little demand was expected. To take advantage of such a situation, the raw materials should be immediately available.

The storage space available also influences the quantity to be purchased. Chemicals, metals, or other raw materials which

require special storage facilities are limited as to the quantity which may be purchased at one time by the amount of suitable space that is available. If conditions warrant, the situation can sometimes be relieved by renting public or private warehouse space.

If the raw material is highly perishable, this factor influences the quantity to be purchased at any given time. The greater the quantity on hand, the greater the loss. The loss on materials such as metals and wood would be slight, but some chemicals and oils are highly perishable and the loss can be a heavy one if special storage precautions are not taken.

The tendency of a material to become obsolete should be taken into consideration in determining the quantity to be purchased. Colors and finishes go out of fashion and raw materials having a color, weave, or finish which is no longer in demand are not usable. Synthetic materials are substituted for natural materials, for example plastics instead of metals, and metals in place of wood. A serious loss can be incurred on heavy purchases of raw material that becomes obsolete.

The interest charge on the purchase of a large quantity of a raw material must also be considered. When interest rates are high this cost is important. Taxes and insurance expense may also be greater if large quantities are purchased. These expenses would depend on the rate of consumption of the raw material and whether or not the inventory increase was insured.

The time to purchase raw materials, like the quantity, depends upon the present and probable future price. It also depends upon the length of time required to process and consume the stock of raw materials on hand. The length of time required by vendors to make delivery also helps to determine when the order for needed materials should be placed.

Many industries are seasonal, that is, production is at a peak during certain months and at a low level in other months. The clothing, furniture, canning, and automobile industries are examples. Raw materials must be ordered and delivered in sufficient time to meet the requirements of production in the peak periods.

The place to purchase raw materials is in some instances

rather definitely limited. The production of lead and copper, for example, is concentrated in a few areas. This concentration is less characteristic of other raw materials, particularly some of the processed materials but even with these there is some tendency to concentration of production. Some materials such as textiles and lumber can be purchased in widely separated places.

If there is choice in the place where a raw material may be purchased, transportation costs to the factory are a prime consideration. In industries, such as the steel industry, the advantage which a near-by source of raw materials may have in the matter of transportation cost is offset by the use of the *basing point system* of pricing. Certain cities and towns are designated basing points. These are usually places of considerable production. Prices are quoted from the basing points and the buyer pays the freight from the nearest basing point regardless of the place of shipment.

The price of raw materials does vary from place to place and often by more than the differences in transportation cost from given points. Some producers overestimate consumer demand while others underestimate it. The degree of demand necessarily affects prices wherever one or the other condition prevails. Important differences in price may exist only a short time until the other buyers discover these differences. Their buying at an oversupplied point brings prices back to their normal relations.

The quality of some raw materials also varies according to the place in which it is produced. Examples are fur, wool, cotton, hides, wheat, and fruit. To the extent that raw materials are bought in more than one producing area, consideration must be given to the quality produced in each place.

Supplies. Those supplies consumed in large quantities are purchased, in general, by considering the same factors as are involved in the purchasing of raw materials. They are normally bought direct from the manufacturer or other producer such as a coal mining company or a petroleum refinery. Supplies consumed in small quantities usually can not be purchased economically or obtained quickly from the producer. Normally a wholesaler will be located nearer to the user so that small purchases can be made conveniently.

Parts. Frequently, the manufacturer may choose whether to make a given part or a sub-assembly of his product or to buy the unit from a parts manufacturer. Parts which are controlled by patents must be purchased from the manufacturer who holds the patent, although the patent holder may sometimes grant permission or a franchise to manufacture his patented unit. The desirability of such an arrangement depends upon special conditions which need not be mentioned here. The present discussion is concerned with those parts which are less closely controlled by patents.

A primary factor in determining whether to buy or to manufacture a part is the cost. Whether or not the quoted price is reasonable can be determined on the basis of a reliable estimate of the manufacturing and delivery costs for the quantity desired. Industrial estimators can often arrive at an estimated price which will closely approach the actual cost of production. When this is done, a sound basis for determining whether to buy or manufacture a part is established.

The simplicity or complexity of a part must also be considered. A simple, elemental part, such as a washer, presents no difficult production problem and the manufacturer no doubt has the facilities for producing it. But he is not likely to have the facilities for producing a carburetor, an electric motor, or other complicated sub-assembly. The production of such parts is specialized and the specialized producer can normally manufacture the part at a lower price than can the manufacturer who uses the part as a sub-assembly for another product.

If the decision is made to buy a certain part, the problem of selecting a vendor is raised. In selecting a vendor, his probable ability to continue to deliver in the quantities desired must be determined. This requires an inspection of the vendor's plant and an examination of his financial statements.

It is important that the parts manufacturer be able not only to deliver the quantities desired, but also to deliver when they are needed. Otherwise, the flow of production is interrupted, the manufacturer is unable to keep delivery date obligations to dealers, and dealers can not deliver to consumers as promised.

Questions

1. What are the four classes of industrial goods? Define and illustrate each.
2. What is the nature of the market for industrial goods?
3. How does the nature of the demand for equipment affect its sale?
4. What middlemen handle equipment?
5. Does a purchasing agent usually have the same authority in buying capital goods as in buying supplies and raw materials?
6. Why do some firms own the sources of their raw materials?
7. What are the two markets for parts?
8. How are supply items sold when they are consumed in large quantities? In small quantities?
9. How is equipment usually bought?
10. What factors should be considered in buying industrial equipment?
11. What executives determine the specific kind of raw materials needed by a firm? What factors should guide them in making their decision?
12. What factors determine the quantity of raw materials to be purchased?
13. What factors determine the time to purchase raw materials?
14. What factors determine the place to buy raw materials?
15. What must be considered in determining whether to buy or manufacture a part or sub-assembly?
16. Purchasing agents often resent being told by shop foremen, department heads, and high executives what brands or makes of products to buy. They claim that these people are too easily influenced by shrewd salesmen, friendships, or personal whims. Purchasing agents argue that they are trained to buy, to evaluate the arguments of salesmen, to judge calmly the qualities of products offered by various sellers, to secure reports from users of the products, and to have laboratory tests made. As a result, they claim to be better judges of the merits of the products offered by competing sellers than are the men in the shops or the offices.

    Evaluate this argument.

III. *Retail Marketing*

A. Organizations

12

The Independent Retailer

INDEPENDENT retailers are by far the most numerous of the different types of retailers and they account for the largest portion of the total volume of business done by retail stores. In some lines, however, this supremacy does not exist and in other lines it has been challenged. This challenge has been met by independent retailers both collectively and individually in several different ways. Who the independent retailer is and what he has done to meet the encroachments of his strongest competitor, the chain store, will be discussed in this chapter.

Characteristics of the Independent Retailer

Most independent stores are small concerns that are owned and operated by the proprietor or by partners. The independent retailer ordinarily has a location more convenient to his customers than do his large competitors. The crossroads, village, small town, and neighborhood city stores are closer to the consumers than are most other stores. Small independent stores in the central shopping district are usually situated at street level where the merchandise can be seen easily by passers-by. Such stores may be on corners, near railway stations, in office buildings, or in other places convenient to potential customers.

The independent retailer usually has a closer personal contact with his customers than do the large stores. The rural retailer calls his customers by name; the neighborhood retailer in

the city likewise knows many of his customers and is familiar with their wants.

The independent store is ordinarily too small to employ specialists in buying, window display, stock display, lighting, advertising, accounting, credit extension, collections, and employee training. Since the owner must handle all these activities himself, they are frequently less well done than in a large store employing a staff of specialists. For example, the small store usually has a higher percentage of bad debts losses on credit sales than does the large store that employs a credit manager. Furthermore, the small store's system of accounting and stockkeeping is usually less detailed, a feature which proves to be a handicap when analyzing store operations and in making purchases. On the other hand, it does not have the cost of keeping elaborate records, nor of employing a staff of high-priced specialists.

In 1939, over one half of the retail stores of this country had annual sales of less than $10,000. These stores did less than 9 per cent of the total business of all retail stores. If these stores were open 300 days of the year, their average daily sales would be $13.20. If the margin of such a store were as much as 50 per cent, it would provide $6.60 out of which to pay for rent, fuel, light, wrapping materials, advertising, delivery, and interest. Some of these small retailers may use little or no advertising, borrow no money and make no deliveries. Even when this is the case, their margin provides a very small profit after other expenses are paid.

Some of these small stores are so located that they are a real convenience to their customers, as, for example, a country filling station, a village drugstore, or a lobby newsstand. Operators of some retail stores perform other services such as serving meals, making hats or clothing, or repairing watches, tires, clothing, automobiles, electrical appliances, shoes, and plumbing. Many of these small stores are conducted in homes and much of the selling is done by the wife or children while the husband is at other work. Individuals who would otherwise be unemployed because they cannot hold strenuous jobs or because they are unable to continue their regular occupations frequently

start their own retail businesses. Such people seldom have training or experience that fits them for retail business.

Independent Retailers Classified According to Location

The problems of the independent retailer vary somewhat according to his location. On the basis of location they may be classified as follows:

1. Rural stores—located at country crossroads, in villages, and in small towns
2. Trading center stores—located in the country seats and smaller cities scattered throughout the country
3. Shopping center stores—located in the shopping districts of the larger cities
4. Neighborhood stores—located in the smaller business districts and residential areas of cities.

Rural stores. Rural stores consist of specialty, multiple-line, and general stores located in villages and on country roads. Many rural stores handle only one line of goods, such as groceries, hardware, building materials, or clothing; others handle groceries and a stock of miscellaneous (variety) goods. Many handle two or more lines of goods; for example: hardware and groceries; clothing, dry goods, and hardware; groceries and shoes; building materials, coal, and farm equipment. Many rural stores attempt to handle all kinds of goods to meet the daily needs of their customers. A typical general store carries such goods as groceries, shoes, work clothing, underwear, hats, hosiery, hardware, stoves, seeds, tools, and some farm and household equipment.

In addition to selling goods, rural stores are often important in assembling such farm products as eggs, poultry, cream, and cotton. One fourth to one half of the total business of some rural stores consists of assembling farm products for shipment to other markets.

The rural store of today has to meet conditions quite different from those which prevailed when the country was being settled. The pattern of settlement in the United States has been influenced directly by horse, water, and rail transporta-

tion. County seats were located 20 or 30 miles apart so that a man on horseback could visit the courthouse and return home the same day. The county seats usually developed into trading centers. Between them villages were established every four to eight miles to serve as assembly points for farm products and as supply depots where the farmers could buy convenience goods and farm supplies. Certain villages also grew into trading centers.

For about two decades after the railroads were built, the farmers bought their convenience goods and some of their shopping goods at the village stores. Other shopping goods were bought on periodic visits to the county seats and on occasional visits to larger cities. Then came the mail-order house with its greater variety of goods and, in many instances, lower prices. The rural stores were forced to reduce their prices and carry wider assortments of goods to retain their customers. After two decades of competition between the rural store and the mail-order house, the automobile came into general use and increased the rural store's competitors.

The automobile and the building of surfaced roads enabled the farmers to visit frequently the larger towns where stores were better stocked. The low-priced specials advertised by these chain and independent stores appealed to the farmers. In some parts of the country there has been an increase in farm tenancy, while some parts have had a decline. The decline in rural population has caused a decline in the demand for many kinds of goods.

Rural stores have several advantages. They are closer to their customers than any of their competitors. They have low operating expenses. The cost of living, the wage scale, and the cost of rent are low in the rural districts. Total expenses are often from 13 to 18 per cent of sales. The rural stores, likewise, usually have little or no cost for delivering goods to the buyers. The rural dealer is personally acquainted with his customers and he often extends credit to them. He may have lower selling prices than the stores in the larger towns because of their lower operating expenses.

The greatest disadvantage of the rural store is its limited

variety of goods. Travel by automobiles, fashion magazines, moving pictures, the radio, and advertisements in the newspapers provide the rural population with the latest style news. There is less difference in the fashions of clothing, household furnishings, and mechanical appliances between the city and country population than ever before. When rural buyers cannot obtain popular styles from the rural stores, the automobile enables them to shop in the larger towns. The rural dealer can partially overcome this handicap by purchasing small quantities of the desired merchandise, by reordering frequently, and by ordering from catalogs when customers want articles that are not in stock.

The rural dealer often lacks a newspaper that is a satisfactory advertising medium. To advertise in papers published in the county seat often involves unnecessary expense due to wasted circulation. If no satisfactory local paper is available, the merchant can advertise by direct mail or by outdoor signs; many rural stores, however, fail to advertise consistently.

Much business is lost by the rural dealers because of indifference, poorly displayed goods, too liberal extension of credit, failure to collect accounts, and inadequate advertising. Perhaps more sales are lost for these reasons than from inherent handicaps in the business.

Generally speaking, the business of rural stores has been declining. The larger towns have many attractions, such as amusements, legal and medical services, banking facilities, barber shops and beauty parlors, schools, hospitals, and repair shops for different types of goods. When people come to a town primarily for such services, they often buy goods. Trade is consequently being concentrated in larger towns, especially the county seats.

Trading center stores. Trading centers are towns that attract customers from the surrounding area. The number of consumers is large enough to enable merchants to handle fairly complete lines of shopping goods. Trading centers vary in population from five thousand people (even less in sparsely populated districts) to cities of 100,000 or more.

Trading center stores consequently are able to carry more

complete stocks of goods than the rural stores. The larger stocks of goods, plus the variety of available services and amusements draw people to the trading centers. The stores advertise in the local papers which often cover the entire trade territory; many of their ads feature low-priced "specials" or "leaders." The trading center retailer has an excellent opportunity to make acquaintance with his customers and to study their needs. Trading center stores draw customers away from the rural stores but lose trade to the stores in the larger cities.

The trading center retailer has higher wage and rent expenses than the rural merchant, and he is located at a greater distance from his rural customers. These factors give the rural merchant the advantage in many sales. After all is said, it is more convenient to buy near home. If the farmer sells his grain, livestock, milk, potatoes, or cotton at the nearby village, the trip to the trading center is an extra trip. Most trading centers are handicapped by limited parking space.

Central shopping district stores. Independent downtown stores are located in the high rent districts. As the amount paid for rent usually increases faster than the volume of sales, these stores have a higher percentage expense for rent than stores located in the smaller towns and cities. Very commonly such stores use the street floor only, which means that they must pay first floor rent for all space occupied. The large store, on the other hand, often has several selling floors and thereby utilizes some lower-priced space. Some small stores are located on second floors or in basements, but in such cases they may have to do a large amount of advertising to attract customers.

The large number of people in downtown districts furnishes enough buyers for different products and encourages a high degree of specialization. Some stores handle only one kind of merchandise: candy, jewelry, men's hats, luggage, oriental goods, periodicals, gift goods, books, tobacco, rugs, shoes, women's hats, sporting goods, office supplies and toys. Furthermore, some sell only one grade of goods; for example, popular-priced candy or expensive hats.

Merchants who specialize in selling a certain product have wider or more complete assortments of the item than do stores

that carry more kinds of merchandise. The shoe store catering to only one class of trade may sell shoes in a variety of materials and styles to fit all shapes and sizes of feet. It thus attracts customers who want distinctive styles or who have trouble in buying comfortable shoes in general merchandise stores. A full assortment of a given article attracts customers because they feel that they can find exactly what they want, can make selections from large stocks, or can obtain distinctive goods.

All downtown stores do not, however, specialize in one commodity, nor do they all carry complete stocks. Drugstores, for example, attempt to handle almost any small goods which sell rapidly. Other stores carry only the fast-selling items and try to make a profit by a large volume of sales and a rapid rate of stock turnover.

The main competitors of the small downtown stores are the large department and large specialty stores located in the shopping districts and also the retail shops located in the suburbs and residential neighborhoods.

An advantage of the small downtown stores in contrast with large downtown stores is their greater convenience. Since the small stores are usually located on the street level the goods are more accessible to passers-by. This is especially important for convenience goods such as newspapers, magazines, cigarettes, candy, and soft drinks and lunches. Ease of entrance is said to be more important to men than to women customers.

Some of the small stores maintain an exclusive atmosphere which the large store patronized by the general public finds difficult or undesirable to achieve. Also, the small store often has a more friendly atmosphere than the large one. Many people like to be served by the owner who frequently acts as a salesman, at least part of the time. Because the other salesmen work under his immediate supervision, the small store often has a better quality of salesmanship than the larger stores.

The small store cannot employ merchandising, credit, and advertising specialists as can its large competitors. It cannot advertise so advantageously, for it cannot afford the large space in the city papers and it cannot afford an expert advertising manager. It does not have the reputation that is often obtained

by a large store. Nor is it able to offer the consumer all kinds of goods as does the department store. It is handicapped in rendering credit service, for it cannot afford a complete credit department. It may not be able to buy as cheaply as the large store, and it does not usually have specialized buyers to scour the market for new and distinctive goods.

Neighborhood and suburban stores. Neighborhood stores in many ways occupy positions midway between the small town stores and downtown stores in city shopping districts. They have higher wage scales than the small town stores. They have a closer personal acquaintanceship with their customers than the downtown stores but not as close a touch as the rural stores. They are located closer to their customers than the downtown stores, but they do not carry an equally wide variety of goods. Neighborhood areas lack many attractions found in the shopping districts. The large number of stores, the variety of goods, the brilliant show windows, the theaters, the restaurants, and the crowds attract many people to the downtown area when they could obtain the goods at the same or lower prices at neighborhood stores. The neighborhood merchants thus have the same complaint against the downtown stores that the rural proprietors have against the trading center stores.

One distinct advantage of the neighborhood stores is the greater amount of available parking space. Traffic congestion and limited parking space keep many people away from downtown stores and help the suburban stores. Many of the large downtown stores have opened branch stores in the suburbs, perhaps because they believe that it is too difficult to draw any more trade into the congested downtown districts.

Special types of stores have also grown up to serve the motorists. Among these are roadside stands, street-side markets, drive-in markets, (groups of stores built around a parking space into which customers may drive and park) and large food markets located outside the business districts. Thousands of roadside stands along our highways sell gasoline, oil, tires, meals, sandwiches, candy, drinks, groceries, novelties, drug sundries, and antiques.

Meeting Chain Store Competition

Chain stores have two major advantages over independent retailers: (1) operating efficiency secured through division of labor and the employment of specialists and merchandising experts and (2) large buying power.

What can the independent do to overcome the advantages of the chain store? He can improve his efficiency and become a better retailer. He can secure a good location for his store, select his goods carefully, display them well, arrange attractive store and window displays, practice good salesmanship, train his employees to give cheerful and courteous service, turn his stock rapidly, keep adequate records, sell for cash or extend credit carefully, collect his accounts promptly, and advertise enticingly. If the independent retailer can do all this and put his own personality and individuality into his business besides, he will compete more successfully with large retail organizations.

Chain and department stores do not undersell independent retailers on all articles. Many independent retailers have adopted cut-price leaders to attract customers to their stores and some independent retailers seem to have used specials to very good advantage, even though they can not always buy them as cheaply as their large competitors. The danger is that they will lose more on the leaders than they will make on the increased sales of other goods. The independents are also often handicapped in advertising their cut-price leaders.

Some independents believe that the chains secure most of their advantage from operating on a cash-carry basis, and that the way to meet chain store competition is to operate on the same basis. This has been successful in some instances, but in many cases it has not enabled them fully to meet chain store prices. Other independents believe that the best way to meet chain store competition is to emphasize credit and delivery service and to give careful attention to the needs and wishes of their customers. No generalization can be made as to which is the better method. Local conditions, the type of customer, and the retailer's own ability are probably the determining factors.

Many independent retailers believe that large buying power is the greatest advantage of the chain store. To overcome this advantage they have organized coöperative chains, voluntary chains, buying groups, and buying clubs.

Coöperative chains. The independent retailers who organize themselves into a coöperative chain usually own and operate a wholesale house and, as a rule, engage in some common promotional activity. In 1939 independent retailers coöperatively-owned 222 wholesale houses; the majority were in the grocery, hardware, and drug trades. To keep operating expenses at a minimum only a few salesmen are employed; instead the retailers phone or mail their orders. The wholesale houses usually carry a rather limited stock of merchandise, sell for cash or offer short credit terms, and give limited service.

The retailers may select price leaders, which are then advertised coöperatively. They may adopt uniform store fronts and the organization may supply its members with merchandising helps, plans for store arrangements, window displays, and advertising copy.

The coöperatively-owned wholesale house can substantially reduce merchandise prices to its retail members. However, it does not offer them as much service as does the private service wholesaler. The retailers must send in their own orders, must pay for the goods promptly, and often must provide their own delivery service. Sometimes it is impossible for the retailer to secure all the goods he needs from the wholesale house.

An important disadvantage of the coöperatively-owned wholesale house is that it is managed by hired employees, although the retailers devote a part of their time to its supervision. The retailers must either take this time away from their retail stores or neglect the supervision of the wholesale house. This management difficulty appears to be a more or less inherent disadvantage of all coöperative ventures. It is also a problem to keep up the interest and the coöperation of the members, and to promote membership drives. Owing to their limited capital, some retailers find it difficult to buy stock in the wholesale house.

It may be assumed that coöperatively-owned wholesale houses buy as cheaply as do other wholesalers. This would mean that

they would have slightly higher cost prices than the corporation-owned chains. It would appear that the low operating expenses and margins of coöperatively-owned wholesale houses would enable the retailer owners to secure goods for 5 to 6 per cent less than they could from service wholesalers, and sometimes for 1 to 2 per cent less than from cash-carry wholesalers.

Very few data are available showing comparative retail prices to consumers offered by coöperative chains and by other types of retailers. The fact that the corporation-owned chains show relatively little price advantage over the independents in some of the larger cities may be due to the fact that some urban retailers have well-organized coöperative buying organizations.

Voluntary chains. Chains of retailers which are organized or sponsored by one or more private wholesalers are called voluntary chains. Such organizations have had their largest growth in the grocery trade. Usually when a retailer becomes a member of a voluntary chain he is required to sign a contract covering his relations with the chain.

The wholesalers usually maintain their outside salesmen, extend credit, and give free delivery to many of the retailers. As a result, they reduce operating expenses little, if any. Their services to their retailers include (1) providing price leaders at a cost low enough to allow the retailers to meet chain store prices, (2) arranging for coöperative advertising, (3) supplying sales and merchandising advice, (4) granting the privilege of using the coöperative's name. The coöperative advertising and price leaders are evidently the greatest advantages to the retailer. The voluntary chain lays much more emphasis on the benefits of the coöperative plan than does the coöperative chain. This perhaps explains the rapid growth of voluntary chains even though they do not supply the retailer with goods as cheaply as does the coöperative chain.

Many voluntary chains employ trained specialists to help the retailers improve their methods and to become better merchants. These specialists may prepare window displays, store layouts, accounting systems, or copy for advertisements. They visit the stores and give advice to dealers. The weakness of such supervisors is that they can only give advice, whereas the

supervisors in the corporate-chains give instructions. Many of the independent retailers do not follow the advice offered by the supervisors. On the other hand, the chain store manager who does not follow instructions is likely to lose his job. In the voluntary chain, the salesmen for the wholesalers are often expected to act as supervisors. These men are primarily salesmen and often make poor supervisors.

Group buying. A buying group is made up of several merchants who select merchandise jointly and place one covering order. In the retail field, group buying is most commonly practiced by department, clothing, and furniture stores.

There are two advantages to group buying: better selection of merchandise due to the combined judgments of a number of buyers, and quantity discounts or lower prices because of the orders' large size. The main limitations of group buying are the differences in the needs of different stores and the difficulty of getting the various buyers to work together. Buyers may fear the loss of their prestige or of their positions and consequently oppose this system of buying. If the stores in a group cater to different classes of trade, it will be difficult to buy merchandise jointly. Since members of a buying group are commonly located in different towns their demands for style merchandise may vary according to the preferences of local consumers. Fashions, however, are becoming more uniform throughout the country. Chain stores and several other buying groups have demonstrated that popular-priced women's wear and men's apparel can be bought collectively. Group buying is important to the department stores located in the smaller cities and in the outlying shopping sections of the larger cities. These stores are often too small to secure the most favorable quantity prices and may not have expert buyers for all types of merchandise handled.

Some stores report that the joint selection of merchandise is the principal advantage of group buying. The buyers meet to inspect the samples and to select the best values offered. Of course, if the buyers make their selections hastily poor merchandise may be chosen. The reliability of the manufacturers and their ability to deliver the quantities wanted by the group

are also considered. It has been thought by some that groups try merely to get the lowest price possible. Such a practice is bound sooner or later to lead to a cheapening of the merchandise; to avoid this danger, groups may decide upon a definite price range and select the best merchandise that is offered within that range.

The group may be able to secure lower prices, however, without sacrificing quality. For example, a dress which has been retailing at $15.75 and which was purchased at $10.75 may, by the larger purchases, be bought for $10. This 75 cents may be kept to increase the retailers' profits, or it may be passed along to the consumers in lower prices. One large department store had been buying a certain type of screen in lots of 1,000 dozen and obtaining 10 and 5 per cent discounts off the manufacturer's price while other stores were getting 10 and 2 per cent, or 7 and 5 per cent off. As a result of group buying, better prices were obtained, particularly by the smaller members. Savings of from 5 to 12 per cent have resulted from group buying. The U. S. Department of Commerce found that women's coat and suit manufacturers gave average discounts of 4.4 per cent to buying groups.

When first organized, buying groups commonly went to the manufacturers and asked for a special price on a certain quantity of goods. The order was placed on the basis of the quoted price. If all goods were needed immediately, the manufacturer might be rushed to make delivery and then find that his business was very slack. When deliveries were made over a period of time, it often happened that the member stores bought less than they had agreed to purchase. The practice was unfair to the manufacturers who, naturally, felt they had been cheated. To avoid this difficulty another method has been developed. The buying group selects what are called preferred resources of supply—manufacturers with whom the buyers are to place all possible business. The manufacturers agree to give a sliding scale of discounts based on the total quantity purchased by members of the group during a given period. For example, a manufacturer of men's clothing may agree to give the following discounts to group members on purchases made during a six

months' period: 5 per cent on sales of $100,000; 7 per cent on sales of $200,000; and 10 per cent on sales of $300,000. The manufacturer is thus enabled to operate his plant more regularly. The stores obtain the merchandise as needed and still receive quantity discounts based on the total purchases of all stores in the group.

A significant development in group buying has been taking place, although the total quantity of apparel merchandise bought in this way is estimated to be less than 10 per cent. Some groups report their greatest success in buying supplies (for example, wrapping paper, boxes, twine, excelsior, tires, and gasoline) and such staples as sheets, towels, and kitchenware.

The buying club. For many years, groups of retailers have coöperated to secure quantity prices. Although the manufacturer may offer a quantity price on fifty cases, one retailer may be unable to use such a large quantity. He therefore contacts other dealers in his town and they arrange to pool their orders. A buying club, however, usually has a formal organization and pools orders for its members more or less regularly. The retailers in the club jointly, or through a buying committee, select the articles for which lower prices can be obtained by buying in larger lots. They may secure quantity prices from wholesalers, or they may buy from manufacturers, farmers' coöperative associations, or brokers.

All the orders may be placed by one member or the retailers may take turns. The appointed buyer may keep the goods in his store until the members call for them or the members may call for them at the freight station. When one member does all the buying it may place a serious burden on him, for the other members may not call for their goods promptly. If they cannot pay for the goods, they may either leave the goods until they get the cash or ask the buying member to trust them for a few days. The only way to be safe on pooled orders is to require the retail members to make cash deposits when the order is placed.

At times the buying club develops so that a part-time paid secretary is employed. The latter may keep a limited quantity of goods on hand or even make deliveries to the club members.

In this case it has begun to operate a wholesale house. Some buying clubs attempt to secure wholesale prices without incurring the expenses of operating a wholesale house, but it is very difficult to do except on a limited number of purchases. The successful buying club may therefore decide to secure and operate a wholesale house.

Advertising. A common form of advertising is that done coöperatively by retail grocers in various localities. Such advertisements generally feature certain cut-price specials to meet the prices of the chain stores. These leaders are often sold by the retailers at or near cost and in many instances are supplied by a wholesaler at cost. The advertisement may feature two lists of articles: first, the leading specials (usually 4 to 8 articles) sold at cost; and second, articles which are good values, but which carry at least small margins.

Many of the retailers are unable to utilize newspaper advertising individually, owing to the small portion of the town from which they draw their trade. However, a number of stores located in different parts of the city can use newspaper space very advantageously. In many cases, the advertising retailers operate on a service basis and feature this service in their advertising. They may also point out that the stores are all "home owned" and ask for trade on this basis. A part of the cost of the advertising is often paid for by manufacturers whose products are featured.

In some cities the coöperating retailers may be concentrated in a part of the city, and so can not economically utilize the daily papers. In such cases, they may use handbills, direct-mail matter, or window signs supplied by a wholesaler.

Other forms of coöperation. Retailers often coöperate in other ways. In several towns they have organized coöperative delivery systems whereby one member supplies the trucks and makes all deliveries for the retail members.

In more than 1,000 cities and towns the retailers coöperate to gather credit information for use in extending credit to the consumers. Frequently these retailer-owned credit bureaus also operate collection agencies to handle slow accounts.

Questions

1. How do you account for the fact that there are so many small stores?
2. Give a classification of retailers according to their general location.
3. Why is the general store typical of rural areas?
4. What are the advantages and disadvantages of each of the following: Rural store? Neighborhood store? Trading center store? Downtown small store?
5. Why is the small store in the central shopping district usually a specialty store?
6. What are the two major advantages which chain stores have over small independent retailers?
7. What can the small independent retailer do in an attempt to overcome the advantages of the chain store?
8. In what trades are coöperatively-owned wholesale houses most common?
9. How are coöperative wholesale houses operated?
10. What is the most important disadvantage of coöperatively-owned wholesale houses?
11. What is a voluntary chain? In what trade have they had their largest growth?
12. How does a voluntary chain differ from a coöperative chain?
13. What are the advantages of group buying? The limitations?
14. What is a buying club? How does it operate?
15. How do small retailers advertise coöperatively?
16. In what other ways do retailers coöperate in attempting to meet store competition?
17. Some individual stores handle only one kind of goods, for example, one brand of candy. Other so-called "specialty" stores, like the drugstore and the hardware store, handle a great variety of goods. The present tendency is said to be toward handling more and more different articles. The arguments are that a greater variety of goods helps to serve the consumers and that additional lines can be handled without proportionately increasing expenses for rent, wages, and light. On the other hand, it is argued that carrying a wide variety of goods means that stocks are limited and incomplete; that many colors, sizes, or styles are not stocked; that many goods become soiled and obsolete before they are sold; and that the store tends to become a "junk shop."

    Evaluate these arguments. How can a merchant determine whether he should add additional lines to his stock or cut out

some of his present lines and specialize on a smaller number of lines?

18. It has been said that the volume of retail hardware business has been declining. One explanation is that the hardware merchants have interpreted the term "hardware" too narrowly—that they have not added new lines to take the places of goods (harness, buggies, and other horse goods, for example) that have gone out of use or have declined in importance. Comment. What lines can the hardware dealers add to their stocks to increase their volume of sales?
19. How do the small stores hold so much of the trade as they do when many of them are inefficiently managed?
20. It is said that stores in many trading centers have broadened their lines to such an extent that few of them carry fully assorted stocks. There is considerable overlapping of stocks between stores. For example, several stores in a town may carry shoes of the same sizes and at the same prices, whereas no store has complete stocks of wide and narrow sizes nor of high- and low-priced shoes. Sporting goods may be carried by the hardware stores, department stores, drugstores, and bookstores, but no store in town may have a complete line. Such a condition does not properly serve the consumers and is said to drive trade to other towns.

    To remedy such a situation it is suggested that the merchants in the town get together and agree on the lines which each will carry. For example, one shoe store will carry narrow lasts in both popular and high prices, and the other stores will agree to handle the very wide lasts, another arch support shoes, and so on. All would handle the popular sizes and styles in the popular price lines. This can be done for all lines of goods, so that buyers will find that they can get practically anything they want in the town. The merchants will secure a reputation of having complete stocks and the town will draw more trade from surrounding territories and will hold more of its own trade at home.

    Criticize this suggestion. Suggest ways of getting the merchants to agree to such a proposal.
21. Can an independent retailer in the grocery field meet chain store competition acting individually? If so, how? If not, why? Would your answer be different for retailers in other trades?
22. Should the independent retailer trying to meet keen chain store competition go on a cash-carry basis or emphasize credit and delivery service?
23. What use can the independents make of price leaders in meeting chain store competition when acting alone? When acting

together with coöperative advertising? How do the independents secure goods to be used as leaders? Can they meet chain store prices on cut-price leaders? It is said that the public compares prices only on a few staple or standard articles, and that if the independents meet the chain prices on these, the public will think they are as cheap on other articles. Comment on this statement.

24. One difficulty with coöperative advertising is that the same articles do not appeal to the customers of all the stores. A low-quality article may not appeal to a retailer with a high-class trade, while a high-quality article may be unattractive to a dealer with a low-class trade. Comment. How should the articles to be advertised as leaders be selected? Is it necessary that all coöperating dealers have the advertised articles in stock? Is it necessary for all stores advertising coöperatively to operate on the same basis—cash-carry or credit-delivery?
25. Do the coöperative, or voluntary, chains have all the advantages of ownership chains? Can you enumerate any places where they are superior to the chains? Any places where they are inferior? Will they enable the independent retailers to hold their own against the chains?

13

The Chain Store

As understood today a chain store system is a group of four or more similar stores which have a common ownership and are centrally managed. The chain store is relatively a newcomer in the field of retailing. Although what was later known as chain stores existed in this country during the first half of the last century, it was not until after 1900 that the chain stores grew rapidly. The chain store was a natural product of the economic conditions which were developing.

Growth of the Chain Store

Some of the largest and best known chain store systems were founded in the last half of the nineteenth century. In 1858, George Francis Gilman began what later became the Great Atlantic and Pacific Tea Company. Frank W. Woolworth opened his first store in 1879. Before the end of the century, J. G. McCrory, H. C. Babcock, John R. Thompson, S. H. Kress, and S. S. Kresge and several others had founded businesses which became chain store systems. It is estimated that by 1900 there were 700 chain store systems with 4,500 stores, not enough to be much of a threat to the independent retailer.

During the next two decades the chains grew rapidly. By 1920 the total number of chain stores is estimated to have been about 49,200. It was during the decade of the twenties, however, that the chains had their greatest growth. The Census of Distribution revealed that in 1929 there were 151,712 chain

stores. This appears to have been the highest peak reached in the number of stores. The chains were responsible for about one fifth of the total volume of business done by all retail stores in 1929. Ten years later there were only 123,195 chain stores but they accounted for 21.7 per cent of the total business done by retail stores.

Causes of the growth of chain stores. What were the fundamental causes of this growth? These causes are to be found in the political, economic, and social conditions which have prevailed in this country. There was freedom of opportunity to open stores, and men like Gilman, Hartford, Woolworth, Penney and others availed themselves of this opportunity by opening stores. Being men of ambition, imagination, and resourcefulness they succeeded.

Freedom of opportunity alone will not explain the growth of the chains. The causes have been largely economic and based on the existing conditions of supply and demand. The factories turned out more and more goods. From 1900 to 1929 the dollar value of manufactured goods increased six-fold. This gigantic supply of goods seeking a market needed large, efficient selling organizations. These were found in department, chain, and mail-order stores. Quantity purchases often secured prices lower than those available to small independent stores.

Demand was also increasing. Measured in bodies to clothe, feed, and shelter, the increase between 1900 and 1940 was greater than in the 280 years following the settlement of Jamestown. The population of the continental United States increased from 76,000,000 in 1900 to 132,000,000 in 1940—an increase of over 73 per cent.

Most chains developed from individual stores started by efficient merchants. Many early merchants tried to operate several stores located in different towns but often they failed because they could not properly supervise them. A man could not be in two stores at once. It was then said that no business could grow larger than could be supervised personally by one man. After 1900 the techniques of accounting management were greatly improved and they helped to make possible the modern chain. Accounting systems enabled the chain owner to check

on the store managers and see that they did not embezzle the owner's money. Accounting records also furnished statistics which the owner used in managing his business. For many years a chain could expand only as fast as it could train managers. With the teaching of business administration in schools and by private employers, more managers became available and new men could be trained more quickly.

A fundamental of successful chain store operation is the rapid movement of merchandise. The motor truck speeded up the physical movement of goods, particularly from warehouse to individual stores. The widespread use of passenger automobiles after 1920 increased the area from which a store could draw customers and made possible larger individual stores. The villager and farmer could easily visit the trading center towns in which the chains had stores.

The chains have made their greatest progress in the sale of foods, variety goods, millinery, shoes, tires, automobile accessories, drugs, tobacco, and women's ready-to-wear. Foods, drugs, and variety goods can be standardized, the individual items have low unit values, and stocks can be turned fairly rapidly. Millinery and women's apparel have a high fashion element. The chains, with their buyers always in the market, can follow fashion trends more closely than can small independent stores. By carrying small inventories in each store and constantly replenishing them from the central market, they obtain a relatively rapid rate of stock turnover. Since the chains often buy goods on long credit terms, their expansion is due partially to their supplier's capital.

The chains have had relatively less growth in the sale of furniture, floor coverings, draperies, plumbing equipment, electrical supplies, jewelry, sporting goods, and photographic supplies. Some of these lines have slow rates of stock turnover and many of the articles have a high unit value.

Decline in number of chain stores. The number of chain stores declined from 151,712 in 1929 to 123,195 in 1939, or about 19 per cent. Total sales of the chains decreased 7 per cent during this decade: from $9,965,000,000 to $9,106,000,000. This was less than the percentage decline in the price level.

The decline in the number of grocery stores and filling stations caused the over-all decrease in number of chain outlets. The number of all other chain stores increased from 87,726 to 92,811.

Table 13–1

PERCENTAGE OF TOTAL SALES OF RETAIL STORES IN SELECTED LINES MADE BY CHAIN STORES IN 1939

(U.S. Census Figures)

KIND OF BUSINESS	PERCENTAGES
Food group:	
Grocery stores (without fresh meats)	32.4
Combination stores (groceries-meats)	38.4
Dairy products stores, milk dealers	41.4
Bakeries, caterers	29.5
General merchandise group:	
Department stores	30.0
Variety stores	86.3
Apparel group:	
Women's ready-to-wear stores	28.3
Millinery stores	54.4
Women's accessories stores	32.0
Shoe stores	56.0
Other retail stores:	
Accessory, tire, battery dealers	45.1
Paint, glass, wallpaper stores	26.6
Drugstores with fountain	27.1
Cigar stores, cigar stands	27.1
News dealers	27.3
Office, school supply and equipment dealers	27.0

There are two main reasons for the decline in the number of grocery stores and filling stations: first, economies in the operation of, and public preference for, larger stores; second, graduated chain store taxes in some states. When the operation of numerous small stores became unprofitable because of taxes or other reasons, the chains either closed them or sold them to the managers and supplied the latter with goods on a voluntary wholesale basis. A considerable number of filling stations were leased to the managers.

The larger chain food stores, known as supermarkets, are often operated on a self-serve basis. Most of them are located outside the congested retail districts to provide parking space for customers. There are economies in operating super-markets

in comparison with small neighborhood food stores. Goods can be delivered to them more cheaply than to a number of small stores. Fewer store managers and sales clerks are required. The percentage cost of rent is lower, because sales increase faster than rent.

In the case of filling stations, there has been a similar trend away from the small one-man station to the super-, or one-stop, station. The consumers seem to prefer them and they are apparently more profitable.

The Anti-Chain Store Campaign

Chain stores were and are stiff competition for the independent retailers. To the extent that the independent retailer was unable to meet this competition the wholesale merchant also was affected. Wholesale merchant and independent retailer therefore joined hands to combat the chain organizations.

Publicity and propaganda against the chains. The efforts of the independents against the chains began to show results in 1925 when bills were introduced in the legislatures of two states for the purpose of taxing the chains out of existence. By 1929, the pressure of the independents and those allied with them was strong enough to cause Congress to authorize the Federal Trade Commission to make an investigation of the chain stores. The Commission discovered some evidence which indicated that the chains had some important advantages, especially in buying. The evidence also proved conclusively that the chains did not have a monopoly of retailing; this evidence was further supported (if it needed support) by data gathered by the Bureau of the Census in 1930.

It may have been more than a coincidence that the antipathy of the independents increased as prices dropped after 1929. Magazine articles, speeches, debates, newspaper advertising and editorials, films, and radio time were used in denouncing the chains. Retail trade associations brought pressure on manufacturers known to sell to chain organizations. Lobbyists struggled to promote state and national legislation which would hamper the chains. Hundreds of bills of different types were

introduced in the state legislatures, all with the hope of impeding the progress of the chains. Those newspaper editors who were coerced under threat of withdrawal of advertising patronage pointed out to their readers how detrimental the chains were to their communities. Few persons escaped hearing or reading that the chain stores were a menace; attempts were made also, to ally the laborer and farmer against them. The campaign was at white heat.

Anti-chain store legislation. The agitation against the chains led to anti-chain legislation in some states. By 1929, twenty-two states had chain store tax laws on their books. In 1933, over 200 chain-store tax bills were introduced in state legislatures. Congress in 1936 passed the Robinson-Patman Amendment to the Clayton Anti-trust Act for the purpose of making price discriminations illegal. The Amendment is of general application but was passed by Congress on the basis that it was an anti-chain store law. Opponents of chain stores have attempted to secure enactment of a federal chain-store tax law. Some would outlaw a chain operating in more than one state.

The resale-price maintenance laws enacted by 45 states were aimed partly, if not largely, at the chains. The first of these laws was passed in 1931 in California. Price-floor laws ("unfair practice acts") were also enacted in several states to prevent the use of loss leaders, especially by the chains.

The anti-chain laws apparently reduced the chains' profits in some states, caused them to sell or close some of their small stores, and perhaps caused them to raise prices in some instances. Speaking generally, the anti-chain laws have not hurt the chains greatly. The chain method of distribution is efficient. It is a labor-saving device—a method by which a given quantity of goods can be gotten to the consumers with less labor and hence at lower cost. Like many other new labor-saving devices it has been opposed.

The chains and public relations. A great many chains were very poor citizens of the communities where they operated stores. They were growing rapidly and their attention was centered on problems of internal management. Many individual chain store managers were active in the affairs of the communi-

ties where they lived. However, until the late 1920's, relatively few chains were active in supporting the communities that supported their stores. As a result of the anti-chain propaganda and hostile legislation, many chains organized active public relations programs to win public favor. Some of the larger department and variety store chains have excellent public relations departments and have been very active in community enterprises. Some of the small chains in various trades have also been active in local civic, charitable, and religious organizations. Others have been inactive or total "flops" as citizens.

Absentee ownership. One of the chief complaints against the chains has been that they are owned and managed by outsiders who have no comprehension nor interest in local community problems. This criticism is leveled at all types of business owned and managed by non-residents of the community. Locally owned chains have escaped much of this criticism. It is hard for a manager in an office in New York, Chicago, or some other city to understand and feel the importance of the problems facing the various communities where he has stores. Only by visiting these towns, sending public relations managers to visit them, and encouraging local managers to participate in local affairs can this handicap be overcome. One complaint, which is sometimes true, is that the chains change their managers too often.

During the past fifteen or twenty years the chains have greatly improved their public relations. In many communities chains are carrying their full share of community responsibilities. Others are not. Many chains could easily improve their community relations.

Organization and Operating Problems

The basic functions of marketing, namely, buying and selling, are the basic functions of a chain store organization. A chain store system must also store and transport merchandise over a relatively broad area. Records must be kept and personnel must be provided. The organization should be designed to carry out these functions on the proper scale. In addition, the

organization must be sufficiently flexible to meet changing business conditions. It is not static, but must be constantly undergoing change or study for prospective changes.

The internal organization of chain store systems. The usual major divisions of the chain store organization are as follows: Buying, store operation (selling), real estate management, personnel management, accounting and finance. In a small chain the owner may select the store locations, hire and supervise the store managers, do the buying, plan the advertising, and supervise the delivery of goods to his stores. Even a small chain must have an accountant. When a chain is only moderate in size the owner usually needs a store supervisor to check on the operations of his store managers and a man to write his advertisements. A moderate-sized chain might have the following organization:

General Manager
- Merchandise manager in charge of buyers for various lines
- Store superintendent in charge of supervisors who check the store managers
- Accountant in charge of records and money
- Real estate manager
- Advertising manager
- Warehouse or traffic manager
- Personnel manager
- Bakery or factory manager (if any goods are manufactured or processed).

The merchandise manager is in charge of buying and in small chains he may also be in charge of sales. When buying and selling are separated, a general store superintendent or sales manager is in charge of selling. This may include advertising and other forms of sales promotion.

The executive in charge of the real estate division is responsible for obtaining locations. Sometimes this division is called the construction division. Its work consists of selecting locations, negotiating leases, purchasing real estate, making improvements in buildings, maintaining buildings, and constructing new buildings. The volume of this work in a large chain is considerable.

One of the responsibilities of the real estate division is to

investigate and report on prospective locations. If the community in which a store is to be located has not previously been investigated, a report on the significant factors relating to the community is made. This is followed by an investigation and report on prospective sites. The ultimate decision may be the result of the judgment of several executives. The problem is to select good locations which will remain good locations for a considerable time or become even more desirable. The various factors to be considered in arriving at a decision on the community and on the sites are discussed in Chapter 17.

The number and variety of personnel problems in a large chain warrant making personnel a major division of the organization. The responsibility and work of the personnel division of a chain are the same as those of a personnel division in any kind of business organization: obtaining, training, and maintaining people for the various divisions of the organization. Several thousand employees are required by the larger chains.

The controller or the treasurer is head of the finance and accounting division. In a large organization, finance and accounting may be separate divisions. When the controller or treasurer is in complete charge, the division is responsible for all accounting, taxes, and legal and general office work.

Large chains have more departments. They may have managers in charge of public relations, legal relations, and industrial relations and each department may have several assistant managers.

Methods of operation. Chains are integrated, that is, they combine retailing and wholesaling, and sometimes manufacturing. The basic principle of a chain is to buy direct from the manufacturers. Chains of four and five stores in the drug or variety field claim that they can do so on most lines. Two or three large supermarkets may be able to buy direct. With small grocery stores it has been said that ten stores are necessary for successful direct buying. Of course, all direct buyers may not receive the same prices because they buy from different factories, in different quantities, and may receive different services. Some buy under the manufacturer's brands and some under their own private brands.

The goods may be delivered to the individual stores in two ways: (1) by drop shipments from the factory to the store, bills being sent to the chain's main office; (2) by delivery to the chain's warehouse and the chain making the deliveries to its own stores. The producer may deliver perishables direct to the individual chain stores. When he does so, there is a question whether the chain operator is entitled to a lower price than the independent retailer who buys in the same quantities. A small chain may not have a warehouse and so use one of its stores for storage of goods. Warehouses are usually operated for groceries, gasoline, and other convenience goods. Variety goods and apparel of various kinds are usually shipped to the various stores in the chain by the manufacturer.

A chain may operate a warehouse more cheaply than a service wholesaler. It has no salesmen to sell its retail stores. Deliveries are usually made on schedule: perhaps staple groceries once a week and bread and other perishables daily. The trucks go out fully loaded and there is little crisscrossing of routes. Since chains seldom operate small stores, few packages are broken and the expense of a broken-package room is largely eliminated.

Buying. The large chain has expert buyers. The majority of apparel buyers are located in New York and other apparel manufacturing centers. In the grocery line, the manufacturer's men call at the buyers' offices. Buyers of fruits and vegetables purchase in a nearby wholesale produce market or may visit the producing areas and buy from the farmers, from coöperative associations, or local buyers. The large grocery chain in a large city often has its freight cars "spotted" on sidings and trucks the goods to its stores, thus avoiding transactions in a central wholesale market.

Although the principal advantage of the chains is often said to be in their buying and other wholesale operations, many independent retailers feel that they are fully as efficient in operating their retail stores and selling the goods to the consumers as any of the chains. The independents have organized coöperative wholesale houses and buying clubs, patronized cash-carry wholesalers, and joined voluntary chains to secure lower

prices to enable them to meet chain store competition. From this it can be seen that the competition of the chains has helped to reduce the cost of distribution.

Store balance. The chains must have an accounting system to insure that their store managers turn in all the money due the chain. Small independent stores do not have this expense. The usual method is for the chain to set its retail prices and charge the goods to the local manager at their selling prices. His bank deposits plus the merchandise on hand should, when checked, equal the value of the goods delivered to him. When the local store manager is allowed to reduce prices to meet competition or when he buys goods locally (as from farmers), great care must be taken to keep the proper records.

Shortages and overages. Shortages result from stolen goods, from spoiled goods, and from mistakes in records. Overages often occur. In a grocery store, many articles are priced at "two for 25 cents," or "three for 50 cents." When a single article is purchased the store gains a fraction of a cent. Goods may have an odd price per pound and a similar gain is made on the purchase of a fraction of a pound. Anti-chain store propaganda has alleged that overages proved that the chains short-weighted or short-changed their customers. Investigations have shown, however, that the chains are neither worse nor better than the independents.

Requisitioning merchandise. The manager of a chain store is usually furnished with some type of check list that itemizes the merchandise available in the chain warehouse or from its various suppliers. From this list he requisitions the goods which he thinks will sell in his store. In other cases, goods are sent to him on the basis of his sales. A newly opened store is usually stocked on the basis of experience in other towns. Sometimes goods are shipped to the store without a requisition from the manager. Chains often did this in their early days with some ludicrous results—for example, sending coal stoves to an Oklahoma town where only natural gas was used. Most chains realize that there are some peculiar demands in every community and that the local manager must be given authority to meet them. If the warehouse does not have the desired

goods he must be allowed to buy them elsewhere. In farming communities eggs and butter may be available at prices lower than the warehouse price. If the manager is not permitted to buy such goods locally, he is handicapped by having to sell them at a higher price than the other stores.

Training store managers. Chain store companies are constantly faced with the problem of obtaining and training store managers. For one reason or another managers sever connections with the chain. They retire, or leave to take positions with other companies, or to open stores of their own. A man with no ambition is undesirable as a store manager. The problem is to obtain managers who will remain with the company a reasonable length of time and who also are prospects for higher executive positions.

General management. Managing any large organization is difficult. A chain of retail stores presents a particularly challenging set of management problems. The stores are located in many towns and are seldom side by side. Management is spread out geographically. Second, the stores are in constant contact with the public and, to borrow a slang expression, "the public is always in their hair." The chain not only has the problem of internal management but also problems of employee relations, customer relations, and community relations.

One of the major problems is the controlling of expenses in an intelligent and practical manner. The largest expense item of a retail organization is that of wages and salaries. An effort to control this item by offering lower wages and salaries than are paid for a similar quality of labor in other organizations will, in general, not succeed. A more intelligent approach is to set up the organization properly and then establish a system which encourages the labor to be more productive. This objective is usually accomplished by employing a relatively high quality of talent in the upper ranges of executives and a lower quality at the bottom of the organization.

A system of controls is fundamental to the successful operation of a chain store company. This system can at the same time be afflicted with weaknesses. Some executives can become overzealous in their insistence on the standard of efficiency with

which the controls operate. Their attitude can result in low morale among employees and poor employee relations.

As well-conceived as the system for operating a chain store company may be, its operation still depends upon the human element. As clear as instructions may be and as simple as a system can be, it is probably not too broad a statement to say that 10 per cent of the employees at any given time will fail to understand the instructions and the system as it was intended that they be understood.

Chain store prices. One method used extensively by chain stores to attain a large volume of sales is to offer lower prices than do competing stores. In general, this requires that the merchandise be bought at lower prices. Large-scale purchasing, efficiency in buying and store operation, and a reduction in the services offered to consumers have been used to reduce selling prices. Methods of buying and operating have been discussed. Many chains have extended no credit and made no free deliveries, that is, they have operated on the cash-carry basis. A number of chains also operate on the self-serve basis. These methods of reducing expenses make price comparisons with service stores somewhat difficult. It has also been alleged that the chains sold principally low-quality merchandise. Numerous chains have operated in the "popular price" lines but so have many independents. It is difficult to make accurate comparisons of quality for apparel, home furnishings, and the like. Even in the food and drug fields it is difficult for the consumer to compare quality. Although the goods may be made by the same producer and according to the same formula, this fact may be unknown to the consumer. For these reasons there have been more arguments than facts on the questions: Does the chain store undersell the independent? How much does the chain undersell the independent? Does the chain undersell the independent when allowance is made for the services rendered by the independent?

Several investigations have been made of the prices of chains and independents in the food field. When the chains were new, they claimed to undersell the independents by 15 per cent. Certain earlier studies showed savings of almost this amount

(without making allowances for services.) When the chains became established in towns, the independents seemed to find ways of meeting their prices or reducing the difference. Several studies made in the 1930's showed that the price differential was much less, in some instances as little as 1 or 2 per cent. During the war and post-war years, shortages of goods and many substitute articles in the stores have made price comparisons even more difficult.

Questions

1. What were the basic causes of the development of the chain store?
2. What factors caused the decline in the number of chain stores after 1929?
3. Why did the refining companies turn from outright ownership of filling stations to leasing them?
4. Why did the supermarkets develop?
5. What conditions favor chain store operation?
6. Describe the anti-chain store campaign.
7. What anti-chain store legislation was passed during the campaign?
8. Is there a Federal tax on chain stores?
9. Has the anti-chain store legislation seriously hampered the growth and operation of chain stores?
10. What are the major divisions of a chain store organization?
11. What are the major problems in operating a chain store system?

14

The Department Store

THE DEPARTMENT store is another institution which is characteristic of our large-scale economy. The central shopping district of practically every city is dominated by these stores. Some of them have national reputations while others are well known throughout a region or locally. Whether their reputation is national or local, it is probably their most valuable asset.

Stores and Sales

A department store carries a wide range of merchandise among which furniture and hardware are often, but not always found. Home furnishings such as draperies, curtains, linens and other household items are almost invariably carried. The merchandise is usually bought by departments and sold by departments. The management of the store is also organized on a department basis. The Bureau of Census does not consider a store with an annual sales volume of less than $100,000 to be a department store, although it may be organized and operated on a departmental basis. These smaller organizations are called general merchandise stores.

In 1929 the number of department stores, exclusive of mail-order houses and some other stores which might have been considered to be department stores, was 4,190. Their sales volume of $3,903,073,897 amounted to 7.97 per cent of the total sales of all retail stores. The average sales per store were about $931,000, but only 580 stores had annual sales which

exceeded a million dollars. The latter accounted for about three fourths of the sales of department stores and they had average sales per store of $5,040,000. Obviously the department store business has been one of large-scale enterprise and high concentration of sales. Furthermore, no opposite tendency has developed.

In 1939 all stores considered by the Bureau of the Census to be department stores accounted for 9.5 per cent of sales of retail stores. Those stores with annual sales of more than $300,000 were doing more than 90 per cent of the department store business. The number of stores was 4,074 and their sales volume was $3,974,998,000. From the low point reached in 1933, sales increased until, in 1946, they were more than three times as high as the 1933 level, and the indications were that they would continue to increase.

Many of the larger department store companies were founded in the period of expansion following the Civil War and they have grown with the cities. Locations were purchased at a fraction of present values and as the population of the cities increased the sales volume also expanded. Other companies, however, have acquired their locations more recently and have had to pay handsomely for them. Some of the larger department stores have organized holding corporations that operate retail stores, wholesale houses, and realty, manufacturing, delivery companies, as well as various other kinds of companies. Some have expanded into other cities and operate a number of stores.

In 1929 the organization of department store chains was proceeding at a rapid rate. More than one third of the stores in operation on December 31, 1929 had been established during the year. Only about one fourth of the stores had been in operation as long as five years. These chains for the most part had grown by opening new stores rather than by acquiring smaller chains. Retail units in chain department store organizations outnumbered independent stores 2,166 to 1,964, but the chains produced only 16.7 per cent of the total sales of department stores. During the next ten years, the number of chain units increased to 2,672 (about 36 per cent.) In 1939 the

chains were doing about 30 per cent of the business of all department stores.

Some of the older and larger department stores have formed mergers or ownership groups with other stores but they do not have the central merchandising and standardization of operations typical of chain store organizations. The stores are managed individually. The group members have neither complete central domination of price policies and methods of operation typical of chains nor the independence of operation typical of independent stores. Most of the ownership groups consolidated their independent New York buying offices, and have bought from 5 to 10 per cent of their merchandise through these offices. The remainder has been purchased by department buyers of the individual stores. In 1939 there were 13 of these ownership groups with a total of 148 stores and sales of $824,065,000.

The basic causes of the growth of the department store are the same as those for the chain store. Both types of stores developed at about the same time. Both depend on large-scale demand and large-scale supply. Both have elaborate internal organizations.

Organization Problems

An examination of the internal organization of a department store usually reveals four major divisions: merchandising, sales promotion, control, and store management.

What the divisions may be depends upon the same factors as those upon which the internal organization of a chain store system depends. Inertia, tradition, personalities and a clear concept of the functions of the organization are all likely to have an influence. As with a chain store, the organization should be designed to provide for the execution of the functions on the scale intended.

A general merchandising manager is in charge of the merchandising division in a large store. This division is usually responsible for both the buying and selling of the merchandise. The general merchandise manager and his assistants make seasonal merchandise plans and budgets, collect and analyze mer-

chandise statistics, analyze fashions, test merchandise, and inspect the merchandise of other stores. In stores with both a main store and a basement store, a merchandise manager in charge of each of these units reports to the general merchandise manager. Since there may be well over a hundred merchandise departments in a large store, from three to twelve departments are grouped in a more or less logical manner, into divisions with a division merchandise manager in charge of each.

Traditionally, a buyer has been the head of the department for which he buys merchandise. He has been responsible for selling the merchandise which he bought, he has had the final authority in hiring and transferring salespeople, and he has been responsible for the profit earned by the department. There has been some tendency to break with tradition and to make the buyer responsible only for buying. The head of the department is then a chief sales clerk who may be responsible to the sales manager or to the store manager. Either the traditional arrangement or the functionalized arrangement will give desired results under the proper management.

The sales promotion division is sometimes referred to as the publicity division. The manager of this division is responsible for the various kinds of advertising, display, and publicity. It is argued that he should have control of personal as well as impersonal selling—that a more co-ordinated effort would result if such were the case. It is also argued that the comparison shoppers should be in the sales promotion division rather than in the merchandising division, since such an arrangement would provide reports which are less biased in favor of the store's merchandising division.

The control division does the accounting and financial work of the organization. The treasurer or the controller, or an individual who holds both positions, is head of the division. This executive is responsible for collecting facts about the business which will aid in making plans for future operations. Although this responsibility is specifically delegated to him, in some organizations the controller has gone farther and assumed the responsibility for making the plans and insisting on their execution. The situation sometimes results in a conflict with

other executives and it has been necessary to point out that the controller's proper responsibility and authority in relation to other divisions is advisory only. The controller is also responsible for collecting such facts as various governmental bodies require.

The store manager is responsible for the maintenance of the physical plant. Usually he supervises the protection and the movement of merchandise and the purchasing of equipment and supplies; he may also be responsible for workrooms and for the adjustment and complaint department. It is not unusual for the store manager to have the personnel department in his division. This department, however, is sometimes considered of sufficient importance to make it a fifth major division of the organization.

Operating Problems

Department stores have numerous operating problems but only two of the more significant ones will be discussed. One of these is the problem of the leased department and the other is the broad problem of costs of operation.

The leased department. In recent years there has been an increase in the number of leased departments, especially departments calling for a high degree of merchandising or professional skill. The millinery department has been a favorite for leasing purposes because of the great fashion risk involved as well as the designing ability and manufacturing skills that are necessary to create desirable hats. Because of the skilled service that is required, beauty shops, optical, photographic, and watch-repairing departments are often leased.

Various financial arrangements are made in contracts for leasing departments. Methods of operation also are varied. Sometimes the store takes the receipts, pays wages and other expenses, keeps the records for the departments, and makes the deliveries. At the end of the month, the expenses of operating the department plus an agreed rental are accordingly deducted and the remainder turned over to the lessee. Sometimes the arrangement has been simply a percentage of profit or sales, or

rent plus a percentage of profit or sales, or a flat rental for the space.

About three out of five department stores have leased departments, but usually only a very small number of the departments in a store are leased. Leasing has been more popular with the middle-sized stores than it has been with the smallest and the largest stores. It is perhaps more than a coincidence that those stores with leased departments have been less profitable than those stores without leased departments.

Between 1929 and 1939 the number of leased departments increased from 4,271 to 13,229. During the years when sales were declining more rapidly than prices, more departments became unprofitable. Store managements, in an effort to stop the losses, turned to leasing those departments which were particularly difficult to manage, but they did not lease their departments to organizations which were leasing departments on a chain store basis. In 1929 there were 3,675 departments which were members of organizations which operated leased departments in chains. In 1939 there were 5,568 departments which were members of leased department chains.

The greatest increase in total number of leased departments was in those departments leased to independent operators. The number of leased departments operated by independents increased from 596 in 1929 to 7,661 in 1939. These independents have often been leading salesmen in their departments. Store managements have believed that by giving an energetic salesman a more personal interest in the department it is often possible to make a given department more profitable or at least to stop losses.

Departments operated by a leased department chain, although under the same roof as those not leased, have often been considered no more than rank outsiders by the store management. There has been a lack of harmony also where the store management has retained a portion of the control of the leased departments. At times the leased departments have had to make heroic efforts to get coöperation from other departments, to get window space, and to have their advertising and promotional work handled efficiently. This is not to say that coöperation

never exists between the leased departments and other departments. The large number of leased departments operated profitably are evidence that, in general, harmony prevails.

Costs of operation. As a group, the expenses of department stores have been higher than the average for all retail stores. Even prior to 1929 expenses were high and increasing while profits for many stores had vanished. When sales volume declined after 1929, operating expenses did not decrease as rapidly. As a matter of fact, between 1929 and 1933 the ratio of expenses to sales for all department stores increased from 28.3 per cent to 32.7 per cent.

TABLE 14–1

PERCENTAGE OF DEPARTMENT STORE EXPENSES TO SALES

(Based on Census Figures)

	CHAIN			INDEPENDENT		
Year	Total Expenses	Payroll	Other Expenses	Total Expenses	Payroll	Other Expenses
1929	24.35	10.21	14.14	29.91	15.88	14.03
1933	27.45	11.32	16.13	35.42	17.45	17.97
1935	24.65	11.25	18.40	32.21	16.45	15.76
1939	*	11.52	*	*	18.36	*

* Data not available.

The independent department stores had somewhat higher expenses than the chains had. In 1933, when expenses were highest, the expenses of chains amounted to about 27.5 per cent of sales while the expenses of independents were approximately 35.4 per cent. Insofar as expenses are concerned the chain department stores in 1929 had an advantage over the independents of 5.6 cents on each dollar of sales; in succeeding years this advantage amounted to well over 7 cents per dollar of sales.

A closer examination of Table 14–1 shows that the greatest proportion of this advantage came from savings in payroll. The payroll cost of the chains in 1939 was 6.8 less per dollar of sales than the payroll expense of the independents. This was a greater advantage than the chains had had in previous years.

In 1929 the payroll cost of chains was 5.7 cents per dollar of sales less than the same expense for independents, and in 1935 the chains had an advantage of 5.2 cents in payroll. The payroll cost of the chains has shown considerable stability; it averages approximately 11 cents for each dollar of merchandise sold. The independents have had a more fluctuating payroll cost; in 1939 it amounted to about 18.4 cents for each dollar of sales.

It might be concluded that either the independents have been overpaying their employees or that the chains have been underpaying their labor. Neither of these conclusions is necessarily true. In 1929 the average full-time employee in an independent department store was receiving $1,269 per year while the average full-time employee in a chain department store was receiving $1,183 annually—a wage difference of about $7.17 per month. By 1933 the average annual earnings per full-time employee in independent department stores had declined to $1,000 while the average wage per full-time employee in a chain department store was $995.00; the wage difference had practically disappeared. In 1939 the average annual wage of full-time employees in chain department stores was $1,225 while in independent department stores the average was $1,257.

TABLE 14–2

FULL-TIME DEPARTMENT STORE EMPLOYEES AND SALES

(Based on Census Figures)

	CHAIN		INDEPENDENT	
Year	Employees per store	Sales per Employee	Employees per store	Sales per Employee
1929	21.4	$12,171	242.2	$8,448
1933	28.9	10,177	196.1	6,102
1939	35.7	12,525	230.0	7,332

Since there has been no extreme difference between the wages of full-time employees in chain and independent department stores, a large part of the advantage which the chains have had over the independents, insofar as payroll cost is concerned, ap-

parently has been due to the chains' more efficient use of labor. Although no perfect basis for comparison is available, the sales per full-time employee give some idea of the increased efficiency with which the chains have used their labor. The sales per full-time employee in 1929 were $12,171 for chain department stores and $8,448 for independents; in 1933 the average for full-time chain employees was $10,177 and for independent employees $6,102. In 1939 the sales per employee in chain department stores were $12,525 and in independent department stores $7,332.

The average independent department store is a much larger institution than the average chain department store. The sales volume and number of employees per independent store have far exceeded the chains; the difference in efficiency of operation (volume of sales per employee) may be partially because of this difference in size. As a store increases in size, more employees not engaged in the main functions of buying and selling are added to the store organization. These have a tendency to increase the expenses of the store faster than sales are increased. Just at what point the addition of more employees will increase expenses faster than sales varies with time and place. At present there is no available information which would indicate when diminishing returns set in, but department store managements should make a concerted effort to obtain this information. In time the chains probably will have the data for their own particular organizations.

One of the causes for the relatively high expenses of department stores is typical of many large companies. The institution becomes so large that it is unwieldy. Much of the effectiveness of store policies has been lost when policy-making individuals are remote from other employees. In the larger organizations men of authority are mere names to many employees and an executive may be unknown outside of his own section.

Relations with Manufacturers

The tremendous sales volume of some of the larger department store companies has already been indicated. As previ-

ously mentioned, by far the greatest proportion of department store business is done by those institutions with more than $300,000 annual sales. The latter necessitates large volume purchases, and in making these purchases the department stores usually go direct to the manufacturer. The scale of the purchases has made it mutually profitable for manufacturer and department store to deal directly with each other and by-pass the jobbers. Profitable though this may be, however, harmony is often lacking in the relations between the manufacturer and the department store.

The manufacturer, in general, has had to seek out the department store as well as other retailers. Consequently, he has occupied a defensive position. Those manufacturers whose knowledge of department store operating methods has left something to be desired have found their relations with department stores none too pleasant. The department store is not always in the most strategic position, however. It is well-recognized that when a store handles the lines of certain manufacturers the store's reputation is definitely enhanced.

Some manufacturers have approached department stores with "We have consumer demand," and the department stores have countered with "Our high reputation in this city is of many years' standing." They have then gone on to the basic question of whether or not the manufacturer's line is sufficiently profitable to risk the store's reputation in handling it. When this question could be definitely answered in favor of the manufacturer, the next step has been to set the distributive machinery in motion. At times, however, department stores have valued their reputation too highly to permit economical distribution for the manufacturer.

One of the first questions raised by a store management when considering a manufacturer's line has been "Would it compete with our private brand?" If the store has no private brand of the line for which a given manufacturer has been seeking distribution, this question, of course, does not arise.

Some manufacturers have followed policies which have incurred the wrath of the department stores. At times, a store may promote and achieve the acceptance of a manufacturer's

brand only to have the manufacturer take away the exclusive distribution privilege and make distribution of the product general. Naturally, the department stores have resented such policies and have fought back by substituting another manufacturer's brand. Because the incident has been repeated frequently, some department stores have become highly skeptical of exclusive privileges for new lines and new brands.

The attempts of manufacturers to establish price maintenance by contract or otherwise have been highly irritating to the department store. A large number of men who constitute boards of strategy for department stores have lived long enough to see that what might be a desirable price for a given manufacturer's line in one city is undesirable in another city. They have also seen that the consumer's idea of a suitable price for a given article has changed, and sometimes on short notice. On the other hand, department stores have demoralized the local market for many a manufacturer by using one of the latter's products as a loss leader. Manufacturers have in some cases, however, followed policies that encouraged price-cutting.

Manufacturers have given little consideration to the fact that increasing numbers of stores have been developing stock control to a fine point in recent years. In some stores the stock control methods are not worthy of the name "system," but the more alert and efficient managements have become keenly aware of the movement of merchandise through the store both in physical units and in percentage of profit. Manufacturers who have approached department stores with no knowledge of general stock control problems or the developments in a given store have experienced difficulty in getting their products distributed by department stores.

Those managements which are extremely alert on merchandise control measures have stopped such uninformed salesmen cold. On the other hand, manufacturers who appreciate the problems of merchandise control have a definite advantage over those whose only object is another order.

Merchandise control involves the balancing of price lines, staples, specialties, sizes, colors, quantities, and design or style. Naturally those manufacturers who have not understood what

department stores have been trying to do in controlling their stock with the above factors in mind have encountered many obstacles in getting distribution through these stores. Some manufacturers have produced their lines with but slight knowledge of the merchandise control problems which must be solved before their goods reach the consumer. With the intense pressure that department stores are exerting to earn profit, however, more manufacturers are increasing their knowledge of merchandise control and its related problems.

Too many manufacturers' representatives have approached department store executives with scant knowledge of the latter's promotional problems. Manufacturers, with an inadequate knowledge of store promotional methods in the past, have been highly susceptible to store requests for an advertising allowance. With some knowledge of the promotional methods used by department stores, the demand for an advertising allowance could have been refused successfully; at least, some manufacturers would have been assured that their advertising allowances were used efficiently in promoting their merchandise rather than used merely as an additional source of income for the department store.

Some manufacturers have had a sound understanding of the promotional methods of department stores. They have also had a clear picture of the various distribution problems of their products, from their own design rooms to consumption by the ultimate consumer. Consequently, they have developed sound promotional plans for department stores and have reaped an increased sales volume. The promotional material of too many manufacturers, however, has consisted of a few unappealing newspaper mats which should never have been produced. It would have been better had the money which was spent in producing them been sent directly to the department store for use as the promotional men saw fit.

Securing distribution through department stores has been facilitated for manufacturers by the establishment of department store buying offices in wholesale markets. These offices are not new. The increased momentum of distribution has caused central market buying offices for department stores,

chain stores, and associations of retailers to come into more prominence.

Questions

1. How many department stores were there in 1929? In 1939? What percentage of the total sales of retail stores did they account for in each of those years?
2. How does a chain of department stores differ from an ownership group?
3. Are the basic causes of the development of the department store the same as those for the chain store?
4. What are the four major divisions of a department store organization?
5. What are the duties and responsibilities of the merchandising manager? The director of sales promotion? The controller? The store manager?
6. What is the work of a department store buyer?
7. What departments in a department store are most frequently leased?
8. What arrangements are usually made between the department store and department lessee?
9. Why have chains of department stores usually had lower expenses than independent department stores?
10. Has the average full-time employee in a chain department store received less pay than such an employee in an independent department store?
11. Have the chain department stores used their labor more efficiently than have the independents?
12. On what matters have department stores had differences with manufacturers? Why?
13. How can a store secure a "feminine atmosphere"? A "masculine atmosphere"? How should a store be arranged to appeal to women?
14. Why do department stores have such a low quality of salesmanship? Do you believe that they could secure better salesmanship? If so, how? If not, why?
15. The services offered by the department stores are abused by some of their customers. This is especially true of the return privilege. How may the stores reduce the percentage of goods returned without losing goodwill?
16. Some have said that the department stores have erred in placing so much emphasis on service. Comment. A few have been successfully operated on a cash basis. Do you believe that more

department stores should go on a cash basis? Could a department store operate on a carry basis and make separate charges for all deliveries? Are the special services, such as writing rooms, lectures on household management, and nurseries, profitable to the stores?

17. It has been said that one trouble with the department store is that it has not attracted enough of the higher type of employees. It has been said that many ambitious young people have thought of work in department stores as "counter jumping" with no opportunities for really worth-while positions. Department stores have many low-paid employees, but, on the other hand, they have many highly paid employees. One department store with 5,000 employees had, in 1940, 600 people receiving from $3,000 to $50,000 a year; 300 receiving from $1,500 to $3,000; and 4,100 receiving under $1,500 (very few under $1,000).

    Many department stores are said to be definitely trying to secure more high school and university graduates. Do you believe that the securing of better trained people will improve the quality of salesmanship and management and lead to more efficient operation of stores?

15

The Consumer Coöperative Movement

IN RECENT years the consumer movement has stirred the emotions, provoked discussion, and has been promising. Consumers have coöperated in the performance of a wide variety of economic services, the distribution of commodities being but one.

Coöperative Stores

Definition. A consumers' coöperative store is owned and managed by consumers with the objective of performing the functions of a retailer more economically than do private retailers. The capital for the store is provided by consumers who purchase shares in the organization. A board of directors is elected from the shareholders and a store manager is hired. Anyone may buy shares in the organization, but, regardless of the number of shares owned, each shareholder has but one vote in the management of the organization. The profits of the organization are distributed to members as dividends on the shares which they own and on the basis of their patronage of the store. For example, shareholders may be paid a five per cent dividend on their shares; the remainder of the profits is then distributed to shareholders in proportion to their purchases at the store. This latter dividend is called a patronage dividend.

The growth of coöperative stores. The first of the modern coöperative stores began in England in 1844 when the weavers

of Rochdale organized to buy their daily necessities at prices lower than those prevailing in established retail stores. A year later, a tailor in Boston induced the members of his labor union to establish the first coöperative retail store in America. The movement progressed very slowly, however.

Quite a few coöperative retail stores were organized during the period of World War I but their lives were cut short by the depression of 1920–21. When employment conditions improved, new stores were organized but not at the wartime rate. Some coöperatives fell into the hands of aggressive labor organizations which were more interested in strikes and boycotts than in coöperative stores. Many members moved away when factories or mines closed, some stores sold on credit and at cost, some failed to establish adequate reserves, and some could not meet the growing competition of the chain store movement. The consequence was that the rate of growth of the coöperative movement slowed down and some organizations experienced a serious drop in membership.

Every State has had a coöperative retail store at one time or another, but the principal development of consumer coöperatives has occurred in Massachusetts, Minnesota, Illinois, and New York—where there are large numbers of immigrants. Between 1920 and 1929 the coöperative movement practically ceased in the Southern States, but in the North Central States the movement gained ground, due primarily to the organization of coöperative filling stations.

Coöperative store associations have had their greatest development in rural sections. In the large cities, retail store associations have made little progress, because chain and independent store competition continues to be too strong for the coöperatives. In cities where the retail coöperative associations have had the assistance of wholesale societies, however, the retail coöperative stores have had more success. The inclination of the city housewife to go shopping and the difficulty of organizing a group actively among city people have continued to hinder the development of the retail coöperative store in urban centers. Urban consumers have been more inclined to form temporary buying clubs in order to obtain savings in purchas-

ing their supplies. The consumer buying club has the advantage of simplicity of operation with little financial risk.

The recession in economic activity following 1929 had a mixed effect on coöperatives. Those organizations with inadequate reserves and indifferent support failed. Bank failures, business failures, and the ensuing loss of savings and jobs caused a great feeling of uncertainty about the future. Consequently, people were very eager for any program which promised to stretch their dwindling incomes. Guided by the enthusiasm and inspiration of leaders, the average membership of retail store associations increased from 303 in 1929 to 407 in 1933. About one-fourth of the associations in existence in 1936 were formed during the period 1930 to 1934.

By 1939 the number of consumer coöperative retail stores had reached 3,230 and they accounted for one-third of 1 per cent of total retail sales. Hay, grain, and feed stores, filling stations, food stores, and general stores that handled food constituted three-fourths of the total number of consumer coöperative stores.

One of the weaknesses of consumer distributive coöperation in this country has been the absence of a strong wholesale organization, but the latter could not develop until the volume of business handled by retail organizations warranted wholesale operations.

During World War I, attempts were made to organize the local retail societies into wholesale societies and by 1920 at least 13 wholesale organizations were functioning. Efforts were also made in 1919 to unite the wholesale societies in a country-wide organization called the National Coöperative Association. The local retail societies were slow in giving their support and the national organization resorted to the promotion of new retail branches. Wholesale branches were also opened in Chicago, Illinois, Hoboken, N. J., and Seattle, Washington. These branches all went out of business in 1921 and 1922. By 1925 only four wholesale organizations remained in operation.

The development of retail petroleum societies and the adverse conditions during the period following 1929 stimulated new activity. In February 1933, eight wholesale societies organ-

ized National Coöperatives, Inc., and established a central office in Chicago. The purpose of this organization was to increase their purchasing power and to bring about more uniformity in purchasing. It was discovered, however, that all commodities handled by the member societies did not lend themselves to pooling and central purchasing. The organization also felt the need for establishing a central advertising service in order to furnish cuts and mats for members in order to popularize and defend the word CO-OP which was copyrighted as the National's trade-mark. During the period of the NRA, the National successfully defended the policy of paying patronage dividends against a charge of unfair competition. The National organization also worked closely with the various federal agencies that dealt with consumer problems. It recommended that a Department of Consumption be established in Washington, D. C., for the purpose of co-ordinating various consumer organizations.

Another large wholesale federation is United Coöperatives, Inc. It was organized in 1930 under the name of the Farm Bureau Oil Company to serve oil associations in Ohio, Indiana, and Michigan. By 1936 this organization was serving farmers' coöperatives in nine states.

Ordinarily, the wholesale societies have been owned by the retail society members who hold the capital stock. The policies of the federated wholesale coöperatives have been determined and controlled by representatives of the member societies. Some of the wholesale societies have established retail branches to serve localities which do not have a coöperative retail store. Since this activity is not entirely consistent with the coöperative movement, local associations are usually formed to take over the retail stores established by the wholesale associations.

Most of the wholesale societies have handled gasoline, oil, and tires. Some of the filling stations have added small stocks of groceries. The trend is for the wholesale associations to handle more household goods. The wholesale societies have also offered auditing, educational, and management services to their retail members.

There has been considerable overlapping and duplication of

wholesale services in some territories, owing to the existence of rival farm organizations each sponsoring its own coöperative. The situation has been further complicated by the existence of purely consumer organizations in the same territory. National coöperatives have required prospective members to submit maps of their trading areas in order to avoid undesirable conflict among members.

Like the retail coöperative societies, the wholesale societies have followed the practice of making patronage refunds, though not always in cash. In recent years the coöperative wholesale societies have followed the practice of declaring patronage refunds but withholding payment for a specified number of years in order to guarantee sufficient working capital.

Objectives and accomplishments. The objectives of the consumer movement in general and coöperative retail stores in particular were stated by the Department of Labor in 1942. At that time it was said, "The immediate objective is economic—to make the pennies go farther, to eliminate the extra cost entailed by extravagant advertising and by high-pressure salesmanship, to handle only commodities of known good quality, and to fill an increasing number of human wants on a non-profit basis. Like the original Pioneers' society, the present-day movement also has a far-reaching social philosophy. Its final aim is to supply every need of life, social and economic, without profit and by united effort."

What success coöperative stores have had in America has been largely in the lower income group. The economic pressure of a low income has forced such consumers to seek for a way out—a condition which has provided fertile ground for developing inspired leaders of the coöperative movement. When the initial enthusiasm has paled, however, coöperative ventures of all kinds have failed. After the first flush of inspiration, the managements of many coöperative stores have been unable to cope with the hard, practical problems of operation. This is no reflection on the organizers and leaders of the coöperative movement. It is merely the statement of a fact which many of the leaders have recognized.

The leaders of the coöperative movement in America have

looked longingly at similar programs in Europe and have painted glowing pictures of its future success in America. To date, however, economic conditions in America have been too different from those in Europe to permit any widespread success in consumer coöperation, at least, consumer coöperation in distribution.

The principal economic reason for being a member of a coöperative association that operates a retail store is to save on purchases which otherwise would be made at private stores. There is, however, no satisfactory amount of statistical evidence indicating what these savings have been. The Department of Labor did gather some evidence on this point for the year 1936. Of the 267 store associations which reported satisfactory evidence, 185 reported savings or refunds to patrons of less than 6 per cent of their purchases. The petroleum associations showed a better record. Of all coöperative distributive associations reporting, 54 per cent paid patronage refunds of less than 6 per cent of sales. A few associations paid average patronage refunds of $19.71 per member while some others paid an average refund of $6.29. The average refund per member might

TABLE 15–1

PATRONAGE REFUNDS OF RETAIL COÖPERATIVE ASSOCIATIONS IN 1936*

KIND OF ASSOCIATION	AVERAGE REFUND PER MEMBER
General merchandise	$18.13
Farm supply	17.89
Petroleum products	13.87
Fuel	12.56
Grocery	8.94
Student supply	6.29
Miscellaneous	19.71

* *Source:* Florence E. Parker, "Consumers' Coöperation in the United States, 1936," *United States Bureau of Labor Statistics, Bulletin No. 659.*

appear to be low, but a comparison of the refund with the annual income of the member would in many cases show the refund to be significant. The year 1936, however, was a fair business year and costs of operation were lagging behind sales. Consequently, the patronage refunds were probably higher for

that year than for preceding years. As costs catch up with sales, patronage refunds tend to decline, and this, coupled with an improvement in the annual income of the members, causes the members to lose interest in the association. Leaders of the coöperative movement have appreciated this fact and as a result have realized that one of their policies must be to promote education in consumer coöperation. To insure proper education in coöperation, the Wisconsin Legislature in August 1935 passed a law which requires that the public school system give courses in consumer coöperation. In 1938 the Legislature of North Dakota enacted a law requiring high schools to offer courses in consumer coöperation.

Causes of slow growth of coöperative stores. Judged by most standards of comparison, the growth of coöperative retail stores in America has been slow. The causes of this slow growth have been numerous but they may be classified into social, economic, and managerial. The social causes are as follows:

1. Individualism of Americans. As compared with Europeans, the typical American is highly individualistic. He has descended from stock that was individualistic enough to sever connections with Europe and emigrate to the United States. Perhaps economic, social, and political conditions are causing him to lose some of this individualism.

2. Mobility of Americans. A consumer coöperative retail store has a better chance of succeeding in communities where the population does not have a high turnover. Americans are not confined by political restrictions to relatively small geographical areas. When they feel the desire to move because of climatic conditions, the possibility of higher wages, or for any other reason, they move.

3. Urbanization of the population. As already pointed out, consumer coöperative stores have had their greatest success in rural communities. The general trend of the population in the United States is toward a higher degree of urbanization.

The economic reasons for the slow growth of consumer coöperative stores are as follows:

1. The relatively high income of Americans. The typical American has had a relatively high income. The small savings

provided by patronizing the coöperative store has not been important.

2. Low prices of other retailers. Chain stores, department stores, mail-order houses and independent retailers have been able to sell as low and lower than have the coöperatives.

The managerial reasons for the slow growth, as well as the failure, of coöperatives are as follows:

1. Inability to keep good managers. Good managers of coöperative retail stores have frequently recognized that they could do better for themselves by operating their own store. Since they are not always strongly indoctrinated with the coöperative spirit, they have ceased working as managers of coöperative stores and gone into business for themselves.

2. Poor locations. The locations chosen for some stores have been too inconvenient to attract business from people who were not members of the coöperative. Members in whom the spirit of coöperation did not burn very brightly patronized stores which were more conveniently located.

3. Lack of reserves. Savings have been paid out as dividends to members and nothing has been set aside as a reserve for times of economic stress. Coöperatives as well as private enterprises are subject to unpredictable business fluctuations. When prices decline, inventory losses will occur whether a coöperative or a private enterprise owns the merchandise.

4. Sales on credit. If either a coöperative or a private enterprise sells on credit, there is a risk that the purchaser will not pay the debt incurred. Selling on credit has been a violation of one of the fundamental principles of coöperative store operation. Violation of this principle has contributed to the failure of some stores.

5. Management by members not primarily interested in the success of a coöperative store. Some stores have fallen into the hands of labor unions whose chief interest was not in the proper management of a coöperative store. The success of the store was secondary to the objectives of the union.

6. Unclean, poorly-lighted, or disorderly interiors. Whether or not the consumer is a member of a coöperative, he appreciates a clean, well-lighted and properly arranged store. When

it is not attractive, neither members nor other purchasers are drawn to the store.

Credit Unions

Closely related to the coöperative distribution of merchandise has been the development of a coöperative method to finance consumer purchases. Like other coöperative organizations, the need for and the greatest interest in coöperative financial organizations has been in times of economic stress when incomes were diminishing, credit was becoming more difficult to obtain, and rates of interest were becoming more burdensome. During such difficult times, inspired leaders have been successful in organizing a great many credit unions among the lower income groups.

The idea of the credit union had its origin in Europe with the development of other phases of coöperation, but the formation of these organizations in the United States was delayed until 1909, when Alphonse Desjardins, a native of Quebec, assisted in the formation of a credit union in Manchester, New Hampshire. Mr. Edward Filene became interested in the movement and in 1909 he succeeded in securing the passage of a law by the Massachusetts Legislature which provided for the establishment of credit unions. A few other states passed similar legislation but even so there were less than 200 credit unions in 1921. In that year, Mr. Filene established the Credit Union National Extension Bureau and a campaign to secure the passage of state and Federal enabling legislation was begun. The campaign was very successful, and by 1935 forty-one states had passed laws that provided for credit unions. In 1934, a Federal Law was passed which provided for the establishment and administration of credit unions by the Farm Credit Administration. State associations of credit unions were formed and in 1934 the Credit Union National Association was created to direct the movement on a national scale.

Credit unions have been most successful where the members have had a strong feeling of community of interest, where the members were known to each other, and where they have been

engaged in the same or closely related occupations. The largest number of credit unions have been formed among employees of specific business organizations. Credit unions composed of the employees of railroads, stores, and public utility companies are quite as common as those whose members are employees of the Federal Government. The membership fees and par value of shares has been kept low; the former often is no more than ten to twenty-five cents, and the latter about five or ten dollars. Members, in line with a fundamental principle of coöperation, are permitted but one vote regardless of the number of shares held. Loans are made to members only and not to officers and directors.

Credit union membership in 1941 was close to 3,500,000. The amount of loans made was approximately $362,000,000. The most popular rates of interest have been 6 per cent and 12 per cent. Not all of the unions have been successful. Although some credit unions have failed, others have reported paying dividends as high as 17 per cent.

Reasons for Success of Credit Unions

Anyone making an objective evaluation of the credit union movement must come to the conclusion that they have been successful. The reasons for their success are fairly obvious. Among them are the following:

1. High rates of interest charged by small loan companies. If a small loan company offers to loan $100 for one year and the borrower agrees to pay the loan in 12 equal installments of $10 per month, the borrower pays $20 for the use of an average amount of $50. This is at the rate of 40 per cent per year. The credit union will frequently make the loan for 6 per cent on the unpaid balance. That is, after the borrower pays each installment of $10, he pays interest only on the amount of the loan he still owes and not on the original amount of the loan.

2. High rates of interest charged to finance installment sales. Furniture, clothing, and other items have been bought under the same type of an arrangement as cash has been borrowed from the loan companies and at much the same rates. It is told

of some furniture dealers that they prefer to sell the consumer furniture at cost on an installment basis rather than sell it at the normal retail price for cash.

3. Banks failed to solicit the small loan business. Just as the banks failed to solicit the financing of automobiles so they failed to make arrangements for handling the financing of other consumer purchases. Consequently, the credit unions developed to meet the need.

4. Ease of collecting the loan. Frequently the borrower agrees to permit the monthly payment on his loan to be deducted from his pay check by the employer and paid to the credit union. This results in small losses on loans.

5. Private business organizations have encouraged the formation of credit unions. They have done so chiefly in order to avoid the difficulties and irritations connected with garnishment of employee wages by small loan companies and retailers who sell on an installment basis. The paternalistic motive is of less importance. Also, some employees believe that the way out of their financial difficulties is to seek higher wages or salaries. Management may exercise some control over this demand if the employee borrows from his company credit union.

Campaigning for Standards

Consumers have long been aware of their inability to judge properly the quality of the merchandise which they purchase. As they have produced fewer products for themselves and bought more items made outside the home, their total knowledge of the merchandise which they consume has not increased. Time has not been sufficient and too much effort has been required for the average consumer to place his purchases under the microscope.

The consumer's failure in this respect was brought sharply to his attention in 1927 by the appearance of the book by Chase and Schlink called *Your Money's Worth*. Readers of the book delighted the authors with inquiries on how to buy more intelligently and in 1929 the authors organized Consumers' Research, Inc. This organization tested merchandise, informed

subscribers to its monthly bulletin of the outcome of the tests, and made recommendations. The deceptive section of advertising and selling plus the general decline in incomes during the next few years contributed much to making Consumers' Research an immediate success. Those advertisers who received the benediction of Consumers' Research saw their sales climb, while those whose products received no recommendation felt the pressure of increased competition.

In 1933 another book, *100,000,000 Guinea Pigs,* by authors Schlink and Kallet was published, and the desire of consumers for more knowledge about the nature of the merchandise that they purchased was intensified. Dissension developed in the Consumers' Research organization and in 1935 Mr. Kallet established Consumers' Union, an organization very similar in operation to Consumers' Research, Inc. In 1932 another former official of Consumers' Research established Coöperative Distributors. The latter was a mail-order house located in New York City and dealt only in tested products sold under the organization's private label.

The bulletins and publications of Consumers' Research and Consumers' Union had a pronounced effect on the general consumer movement. These publications reached school libraries, women's clubs, and other consumer groups as well as individuals. Their contents were discussed and criticized. Political and economic conditions were right for attempts to secure the passage of legislation which, if it did not protect the consumer, would at least provide more information about the merchandise being sold.

The first point of attack was the Food and Drug Act of 1906. It was charged that this law was inadequate to meet the changed conditions. Mr. Tugwell, the Assistant Secretary of Agriculture, supported measures to revise the law, and the Food and Drug Administration bent its efforts to secure the support of women's clubs and other organizations interested in the establishment of more adequate standards for consumer goods. Periodically for five years, the subject was hotly debated in Congress. The supporters of consumer organizations charged that the proposed legislation was not drastic enough; on the other

side were the advertising interests and producers of proprietary medicines, cosmetics, and branded foods. Finally, in 1938 a new food and drug law was passed which strengthened the Food and Drug Administration but did not provide for the compulsory grading of foods and drugs.

When the National Industrial Recovery Administration was organized in 1933, provision was made for a Consumers' Advisory Board which was to have a voice in the councils of NRA. Attempts were made to require food canners to label their products with grade A, B, or C. The President was interested in the demand for compulsory grade labeling but the framers of the codes ignored the requests of the consumers and grade labeling was not adopted.

To give a voice to consumers in the Agricultural Adjustment Administration, a body known as Consumers Counsel was formed. It represented the consumer in the hearings on agricultural marketing agreements and issued advice to consumers in bulletin form. Other government bureaus which have been interested in establishing standards have been the Bureau of Agricultural Economics and the National Bureau of Standards of the Department of Commerce. The results of the work of the Bureau of Standards, however, have been available only to governmental organizations and not to the public. The failure to make public the results of the work of the Bureau of Standards plus the continued efforts of a wide variety of consumer organizations have generated some demand to establish a government department to be called the Department of the Consumer. The function of the proposed department would be to accomplish for consumers what the Department of Commerce has done for business and what the Department of Labor has done for labor.

Let it be said to the credit of the Great Atlantic and Pacific Tea Company that when the Consumers' Advisory Board was urging grade labeling that company coöperated and labeled some of its canned goods according to grades A, B, or C. The two large mail-order houses—Sears Roebuck and Montgomery Ward—have for years operated testing laboratories to discover facts about the many products which they have offered con-

sumers. In 1934 the American Standards Association—an association formed for the purpose of establishing uniform standards for industrial goods—organized the Advisory Committee for Ultimate Consumer Goods.

Consumers, however, have been skeptical of those organizations to promote the establishment of standards which have not been formed and operated by consumers. In 1937 Consumers Foundation was established for the purpose of harmonizing the interests of business and consumers, but it developed that this organization was really backed and financed by the Institute of Distribution, an association of large-scale distributors. At the New York World's Fair was a Consumers' Interests building for the ostensible purpose of giving representation to the interests of the consumer. It turned out, however, that the building was under the supervision of the Associated Grocery Manufacturers of America.

The Promotion of Coöperation

The coöperative movement has not, like Topsy, just grown. It has behind it almost one hundred years of inspired and enthusiastic promotion. More than once the coöperative movement has almost ceased to exist, but fervent leaders kept it alive.

Perhaps the most important and most active organization in spreading the doctrines of coöperation has been The Coöperative League whose constitution was adopted March 18, 1916 in the home of Mr. J. P. Warbasse, a surgeon of Brooklyn, New York. Immediately after its organization the League began the publication of a monthly official organ and during its first year printed and distributed over 100,000 pieces of literature. By 1924 the League was in full swing. Thousands of pieces of literature including pamphlets, books, letters, magazine articles, and speeches were written and distributed among those who would hear of coöperation and among those whose interest in coöperation might be flagging. Training schools were conducted and delegates were sent to conventions in order to build a solid foundation for coöperation. Attempts were made to

introduce courses in consumer coöperation in colleges and universities but these efforts met with success only after much sustained effort.

As the radio developed this medium was employed and by 1939 national and local programs dealing with some phase of coöperation were an almost daily occurrence. Youth organizations were formed on the basis of what all youth is interested in—recreation—and from recreation members of these organizations have been led to education in coöperation. Even in the display of merchandise the managers of coöperative retail stores were urged to inject in some manner the ideals of coöperation. The field force traveling among the stores was trained in such a manner that their educational functions were placed ahead of their merchandising function. The seal of the League made a wide appearance.

In its educational program The Coöperative League had the assistance of such lesser leagues as the Northern States Coöperative League, the Eastern Coöperative League, the Central States Coöperative League, the Coöperative Youth League, the Coöperative Recreation Service, and a great number of local associations.

The Legal Status of Coöperatives

The earliest coöperatives were organized with little or no consideration for their legal status. They might be an unincorporated association. If so, the coöperative could make no appeal to the courts as a body; furthermore, each member of the association was subject to unlimited liability as were single proprietors and members of partnerships. As incorporated societies, coöperative members would have limited liability, voting would be according to number of shares owned, and shares would be transferable so that a few members could obtain control. This also was undesirable. Consequently, a part of the efforts of the leaders of the coöperative movement has been devoted to securing the passage of laws providing for the organization and management of coöperatives. They have also fought attempts to tax and restrict the coöperatives.

By 1937 thirty-five states had passed laws which related specifically to coöperatives. Some of the statutes have defined what shall constitute a coöperative but the majority have not provided any definition. In general, the kind of business in which a coöperative might engage has not been subject to much limitation. Some states have simply provided that coöperatives might carry on any lawful business. The laws in certain states permit as few as three persons to incorporate a coöperative; other states require as many as twenty-five incorporators. All the laws except the Nevada statute have provided for associations with capital stock. A few states have put a limitation on the par value of the shares, and some states have limited the amount of stock that an individual may hold. In certain states liability of a shareholder has been limited to the amount unpaid on his stock subscription. In other states liability has been extended somewhat, but usually it has been in relationship to the amount of stock held. Most of the states have provided that a shareholder shall have one vote regardless of the number of shares held. Voting by mail or by proxy has not been in general favor although some states permit it under certain conditions. Sixteen states have mandatory provisions governing the distribution of earnings while eight others have suggested procedures for distributing earnings. Some states limit the dividend rate payable on shares. Montana and New York have provided penalties for violation of their statutes.

By 1935 thirty-seven states had passed laws which regulated credit unions. There has been more similarity among these laws than has been the case with the laws regulating other coöperative associations. This has been due in a large measure to the activity of the Credit Union National Extension Bureau which was instrumental in getting many of the laws passed. There is still, however, considerable difference in the provisions of the various laws.

In California as few as three people can incorporate a credit union while in Massachusetts a minimum of twenty incorporators is required. Several states have placed no restriction on

the field from which credit unions can draw membership but almost as many have limited the membership to those having a common bond of occupation or association. Credit unions in Utah are permitted to conduct a general banking business; in Illinois, credit unions have been expressly prohibited from doing so.

Credit unions usually have been given the general corporate powers of acquiring property, making investments, and borrowing money, although restrictions have usually been placed on the investing and borrowing powers. Most of the states permit credit unions to receive deposits from members only; in no case has the making of loans to nonmembers been permitted. Ordinarily the power to make loans has been limited to loan-making for productive and provident purposes. The rate of interest usually has been limited to one per cent per month on balance. It has also been customary to require that a certain percentage of net earnings be placed in a reserve fund.

What Coöperatives Can and Cannot Do

Much has been promised to the consumer by the leaders of the coöperative movement. Something has been accomplished, but not as much as had been expected. The enthusiastic fervor of coöperative leaders has often blinded them to economic and human realities. They have demonstrated that they can accomplish the following:

1. Spread the doctrine of coöperation. Much of the success of the coöperative movement has been due to the evangelical inspiration of the leaders of the movement. The inspiration which these leaders have provided has paled with time. Realizing this, the leaders have made education in coöperation a fundamental of the program with somewhat satisfactory results.

2. Secure the passage of laws favorable to coöperation and prevent the passage of unfavorable laws. They have secured the passage of laws which enabled the coöperatives to organize. They have opposed laws which placed a tax on coöperatives.

3. Promote the adoption of standards. They have continu-

ally agitated for government standards for consumer goods. Although their efforts have accomplished but little, they have helped bring about the placing of more information on labels.

4. Reduce the cost of borrowing. For the small borrower the cost of obtaining funds has been reduced through the formation and operation of credit unions.

It has been demonstrated that coöperatives cannot accomplish the following:

1. Make large savings in the operation of retail stores. The practical failure of these stores in the United States after more than a century is evidence that no important saving has been made. Such statistical evidence as is available also supports this conclusion. If the general level of income increases, there is less possibility that coöperative retail stores will have any important degree of success.

2. Succeed in carrying on any economic endeavor unless tangible evidence of an appreciable saving over a period of time can be shown. The claims of the leaders have seldom been attained in actual practice.

Questions

1. What is a consumers' coöperative store?
2. Explain the two types of dividends which coöperative stores pay if they are successful.
3. Describe the growth of coöperative stores.
4. In what States have coöperative stores had their principal development?
5. What effect did the business recession following 1929 have on coöperative stores?
6. How important were coöperative retail stores in 1939?
7. What are the objectives of the consumer movement as stated by the Department of Labor in 1942?
8. What have been average patronage refunds in various kinds of coöperative stores?
9. What have been the social causes of the slow growth of coöperative stores? The economic causes? The managerial causes?
10. What is a credit union? Describe the growth of these organizations.
11. What have been the reasons for the success of credit unions?
12. Describe the campaign for standards.

13. What methods have been used to promote the doctrine of coöperation?
14. Why was it important to secure the passage of special laws applying to coöperatives?
15. What can consumer coöperative associations accomplish? What can they not accomplish?

B. Starting a Retail Store

16

Becoming an Owner of a Retail Store

A BEGINNING in retailing may be made by acquiring an established store, buying a part interest in an established store, or opening a new store. The chief advantages of owning a store are independence and a higher income. Perhaps it should be said "the *possibilities* of a higher income." There are certain qualifications for the successful ownership and operation of a retail store.

Qualifications for Store Ownership

The primary qualifications for the successful ownership and operation of a store are managerial ability, capital, and knowledge of merchandise.

Managerial ability. The successful independent retailer knows how to manage people and he has a knowledge of merchandising. He is able to attract customers and to secure efficient employees. He is able to buy the articles needed by his customers at prices permitting their resale at a profit. He must buy the right articles, in the proper proportions, and have adequate stocks on hand to meet the customers' demands. He has a bookkeeping system which furnishes the necessary facts with which to operate his business efficiently. He knows how his goods should be priced and displayed. He has new goods on hand before stocks are exhausted. He selects a good location and arranges his store for efficient operation.

Perhaps an enumeration of the owner's responsibilities makes

his work appear complicated. The explanation and discussion of these operations in later chapters will show that each taken by itself is relatively simple. It is the efficient control of all of them at once and under varying conditions that takes managerial ability.

It is sometimes assumed that a person does or does not have managerial ability. This assumption needs two modifications. First, there are various degrees of managerial ability. Most people have some of it and a few have much of it. A retail store can be operated with some success without high degree of managerial ability. The man who has all the required managerial traits in a high degree is the man who will perhaps become the manager of a chain of stores or a large department store. A small store may be operated profitably by a man who has the necessary abilities, developed to a moderate degree. Secondly, managerial ability can be developed. Many people who are not capable attempt to operate retail stores. On the other hand, there are many people who have the requisite ability but who never try to operate stores. Many of these do not know that they have the ability and it is difficult to predetermine who has the necessary ability.

Capital. The amount of capital needed to operate a store depends upon several factors among which are the volume of sales, whether or not the building is owned, and the amount of credit extended to customers. A large store needs more capital than a small store. The prospective retailer usually asks such questions as: "How much business can I do on my capital?" and "How much capital do I need to do a given volume of business?"

Hardware store as an illustration. It may be assumed that a hardware store's owned capital is equal to 45 per cent of its sales. It may be estimated that something like one fifth or one sixth of the average owner's capital is tied up in real estate. Therefore a store that does not own its building should have sales that are nearly three times as large as the owner's capital. A man with $5,000 capital who does not own his store building should sell $15,000 worth of goods a year.

The number of times the average inventory is sold during a

period of time is the rate of stock turnover. This rate affects the volume of sales which a dealer can make with a given amount of capital. If the average rate of stock turnover for a group of retailers is 2.2 times per year and a better-than-average retailer turns his stock 2.7 times, the latter merchant can obtain 23 per cent more sales. The dealer who does not own his building and turns his stock 2.7 times per year, could sell approximately $18,450 worth with $5,000 capital.

The retailer who sells on credit needs more capital for a given volume of sales than does one who sells on a cash basis only. A store with $15,000 annual sales, doing about 40 per cent of its business on credit, and having 90 days credit sales on its books, does some 10 per cent less business with a given amount of capital than the store selling for cash only. It is thus estimated that a store dealer who rents his building, turns his stock 2.7 times a year, and sells for cash, could have sales of $19,000 to $20,000 for each $5,000 capital.

A new store should not plan this closely, however. Sales may develop more slowly than expected. The new store may run into unexpected difficulties and may need additional reserve capital to take care of them. Some stores require more than $20,000 in sales for the most efficient operation, but this sales volume seems to require a minimum capital of at least $5,000. It should be remembered that this is a minimum for a store operated more efficiently than the average store.

What can a store do with $5,000 *capital?* Some stores have margins of 25 to 30 per cent between the cost of the goods and their selling prices. A store with sales of $20,000 a year, and a margin of 28 per cent pays $14,400 for the goods sold during the year. If it turns its stock 2.7 times a year, the average value of goods on hand (at cost) is $5,333. This value is $333 more than the $5,000 capital. The ordinary terms in the trade may be 2 per cent discount if paid within 10 days after date of invoice and the net to be paid within 60 days. The retailer who does not take cash discounts is handicapped in meeting competition, but this may be a handicap that a new retailer with limited capital must bear while he is getting his store established.

Suppose this retailer buys $3,000 worth of goods for cash, the rest, $333, on credit and uses the remaining $2,000 for store fixtures and operating expenses during the first few months. Although he expects to sell $1,666 a month, he must, of course, allow for seasonal variations. Many stores have a smaller sales volume in January and February and a larger volume in March, April, and May. However, he ignores this seasonal factor and expects to sell $1,666 each month. If he does, he will sell $3,332 worth of goods during the first two months. As he is selling for cash he will have $3,332 cash receipts. Of this amount, $2,400 will be used to pay for goods, leaving $932 for operating expenses and credit payments.

These goods, which sold for $3,332, cost the retailer $2,400. The retailer will, during the first two months, buy additional goods worth $2,400, most of which will have to be bought on credit. Once he catches up on his payments he will have monthly sales of $1,666 and, ignoring seasonal variations, he will buy $1,200 worth of goods and have $466 for expenses and profit and for increasing his stock.

Will this plan work? It has been shown that a retailer with $5,000 capital can have sales of $20,000 per year if he turns his stock 2.7 times a year and sells for cash. Very few new stores attain their expected sales within the first few months, or even within the first year or two. It usually takes time to build up trade. There also may be many unforeseen contingencies. Business may slump—for example, the chief industry in the town may close, leaving many of the store's customers unemployed. The prices of farm products may decline, or unexpected competition may develop. In view of these and other possibilities, the man with $5,000 capital should not buy a $5,000 stock of goods.

The retailer opening a new store should have enough money to pay cash for the beginning stock and for his store fixtures, and have some money left with which to pay operating expenses until the store is established. The retailer starting a new store with $5,000 capital should buy about $3,000 worth of merchandise and pay cash for it. This stock indicates a business conservatively estimated at $10,000 to $13,000 per year. If the retailer puts $3,000 in stock he will have $2,000 for fixtures and

operating expenses. If he puts $1,000 into fixtures, he has $1,000 for paying operating expenses until he has his business established. Operating expenses may include wages for himself, rent, heat, light, insurance, advertising, etc. A store of this size is too large for one man to operate by himself. He will need help at busy times and to make deliveries, and also to tend the store during necessary absences of the owner. If members of his family can help at such times it may be possible to get along without hiring extra help.

What are the possibilities of a small store? It is admitted that many successful stores have started with less than $5,000 capital. In many cases the wholesalers furnished much of the capital by extending long credit. In other words, the jobbers carried those retailers who they thought had ability.

If a retailer and members of his family can find a location that is not overcrowded, they may buy a small stock—perhaps only $2,000 or $3,000—and if they have ability, industry, and frugality they can eventually build a successful business. This may be done in a growing neighborhood or suburb that does not yet have a store of the particular kind in which the retailer is interested. The store can turn this stock fairly rapidly, reinvest its profits, and grow up with the community.[1]

Source of capital. By capital is meant the amount of money which is invested in the business. It does not necessarily all belong to the owner. He may have relatives or friends who will become his partners or who will make him a long-term loan. Or, he may be able to borrow on a long-term real estate mortgage or on a life insurance policy.

Knowledge of merchandise. The operation of a store should not be attempted until the operator has a fairly good knowledge of the merchandise which he proposes to retail. Merchandise is of many qualities and many uses. The retailer should be able to tell his customers about the various uses of the different kinds of merchandise which he handles. He should be able to explain the differences in quality between differently priced articles. In

[1] The procedure explained above for a hardware store may be applied to other kinds of stores. The figures would not differ greatly for other kinds of stores with similar rates of stock turnover.

order to acquire a knowledge of goods, it may be necessary to work for a few years in a retail or wholesale store.

There are, of course, instances where men have become successful retailers without previous experience in the particular trade in which they operate. These, however, are the exceptions. The only safe way is to obtain a thorough knowledge of the merchandise before trying to operate a store.

The amount of knowledge required for successful operation of a store varies with the operator's previous experience, with the type of store to be established, and the help received from wholesalers. A man who has successfully operated another type of retail store knows merchandising; he needs only to acquire a knowledge of a particular kind of merchandise. This takes much less time than it does for a man to study both the fundamentals of business operations and the merchandise itself.

If the retailer can have the assistance of a wholesaler who provides plans for store layout, store and window displays, amount and kind of stock to carry, advertisements, and who sends a supervisor to visit the store periodically to help with these problems, he does not need to know as much about store operation and merchandise as the retailer who buys from wholesalers or manufacturers who do not render these services. In fact, one wholesaler operating a voluntary chain believes that a retailer using his services and specializing in his kind of merchandise can become a successful retailer without previous experience.

A new salesman often receives instructions about the merchandise from the owner or an older salesman. He learns on the job. There are several sources of information that will help him learn faster. First, he can study the trade journals. These have articles on the display and sale of merchandise. Perhaps more important are the advertisements in these journals, which picture and describe many goods. Next, manufacturers' catalogs and descriptive leaflets packed with the goods can be secured. Trade associations and wholesalers also put out manuals, check lists, and catalogs. If some of these can be secured, the salesman will have an abundant supply of information about the goods he is selling.

Buying an Established Store

There are several advantages in buying an established business. Among them are the following:

1. The owner may be willing to sell at a price that is very advantageous for the buyer. The owner may wish to sell because of ill health, a desire to retire, or for other reasons. To enable him to locate a purchaser quickly, he offers the business at an attractive price.

2. The established store may have a stock of goods adapted to the needs of the community, particularly if it has been a successful store. This is an advantage to the beginner as it saves him the work of selecting an entire stock of goods for a new store.

3. The established store has an established trade. Many of the patrons will continue to trade with the newcomer. This saves the time usually required to build up trade when a new store is established. Even though the store has not been an outstanding success, some regular customers are an advantage to the newcomer.

4. If the new owner has little or no knowledge of the merchandise, he may buy a store with the agreement that the former owner will remain for a period of time to teach him the business. If there are accounts receivable which the new owner does not want to take over, this period gives the previous owner an opportunity to collect them. The new owner must learn what items are in stock, where they are kept, the demands of the store's customers, and where and how the goods are purchased.

However, there are also several disadvantages to buying an established store. Some of them are as follows:

1. The store may have a poor reputation for goods, or prices, or the people of the community may dislike the former owner. Much of this ill will attaches to the store and it takes time for a new owner to overcome it.

2. The building may be too large or expensive.

3. The location may be poor.

4. The fixtures may be too expensive.

5. The stock may be poorly assorted or unsuited to the needs of the community.

The arrangement whereby the former owner remains for a while as a teacher is usually satisfactory if he has been a successful retailer. If he has been a failure, however, he may teach the new owner poor methods of buying, stockkeeping and selling.

Although the former operator's venture in retailing may have been a failure, the merchandise inventory and the equipment may be still of considerable value. When the prospective new owner discovers that the business has been none too successful, he should look over the store and its location very carefully. Previous lack of success, however, does not prove that the store should not be bought. It is not unusual for a new owner to transform a mediocre or failing store into an outstanding success. Some men have the particular abilities required to effect this change. They make a practice of buying failing stores and selling the business once they are operating efficiently and profitably.

Valuing the inventory. The merchandise inventory is usually valued at its cost or at present market prices, whichever is lower. In some stores the cost and quantities in stock may be determined from the books. The new owner, however, should take a physical inventory before he completes the purchase. If the price tags on the boxes, drawers, and individual articles do not contain cost prices, these will have to be filled in from old inventories or from present catalogs.

After the inventory has been taken, the merchandise should be inspected to determine its condition. The age of the merchandise may be judged by the appearance of the boxes, and packages, as well as by the condition of the merchandise itself. If the new owner is not experienced in making such judgments, he should obtain competent assistance in order to spot obsolete articles. A jobber's salesman may help in order to obtain a new customer.

Because of the importance of merchandise and the large amount of money which it represents, great care should be taken in making purchases. The prospective owner should not hesitate to employ the services of an expert to assist him in placing

the correct valuation upon it. To buy an overvalued inventory and then take losses on it while correcting the condition, means starting with a serious handicap. Many stores have accumulated merchandise which is either unsalable or which sells very slowly. The buyer should therefore be careful in assuming that the inventory is worth its book value. Many articles in a store are subject to rather large price changes in a relatively short time.

Buying receivables. The general advice to the new retailer is not to buy the accounts receivable. Buying them ties up capital and many of them will prove uncollectible. There are times, however, when it is necessary to buy the receivables. If the business is bought from an estate, or from a man who is retiring on account of ill health, the seller may insist on selling the business as an entity.

When a business is acquired by a new owner, the task of collecting money owed to it is more difficult. It is often desirable not to publish that there has been a change of ownership until most of the receivables have been collected. If some of the customers of a store know that it has changed hands, they are reluctant to pay their bills.

In appraising receivables, the new owner should remember that the chances of collecting an account decline with its age. The best customers pay their bills promptly. The older the accounts, the larger the proportion which will not be paid. There seems to develop a feeling among persons of questionable honesty that "We have gotten away without paying it this long, maybe we won't have to pay it at all." One study shows the following as the chances of collecting accounts:

AGE OF ACCOUNT	PER CENT COLLECTIBLE
Under 2 months	99½
2 to 6 months	89
6 months to 1 year	67
1 to 2 years	45
2 to 3 years	23
3 to 5 years	15
Over 5 years	Practically none

Accounts can then be divided by age and valued as follows:

AGE OF ACCOUNT	PER CENT UNCOLLECTIBLE	VALUE PER DOLLAR
Under 2 months	0	$1.00
2 to 6 months	11	.89
6 months to 1 year	33	.67
1 to 2 years	55	.45
2 to 3 years	77	.23
3 to 5 years	85	.15
Over 5 years	100	.00

The buyer may value receivables on this basis, but he should remember that he will also have collection expenses. The latter vary, but collection agencies commonly charge 15 to 25 per cent of each account they collect in amounts up to $500; if legal action is necessary, the charge may be higher. Accounts of less than 60 days may be taken at their face value. Older accounts may be valued approximately as shown in the preceding table less the estimated expenses of collection.

These figures are only averages. Local conditions should also be considered. For example, if accounts are owed by a farmer and the farmers have had crop failures or exceptionally low prices, his accounts, even though one or two years old, may be much better than indicated by the foregoing figures. In the Cottonbelt, for instance, if the farmers have had poor crops or low prices, the dealers may not hesitate to carry them for one or two years.

Another method of valuing accounts is to review each account individually and find out if each debtor still lives in the community. If not, the present addresses and financial condition of the debtors should be ascertained and, if possible, whether or not the account is disputed.

Valuing fixtures. The first problem in valuing the store's equipment and fixtures is to determine their suitability for the new store. If they are obsolete, they may be worth little, regardless of their cost and present physical condition. If they are suited to the new business, their original cost less depreciation figured at approximately 10 per cent a year can be used as a method of valuation. This does not, however, always give a fair value. If the fixtures are suited to the new store and are in

good physical condition, they may be worth almost as much as their original cost. If they are more expensive, or more elaborate than the new owner needs or wants, he will probably estimate the amount which more modest fixtures would cost, and offer this amount, less depreciation. Another factor to be considered is the change in market prices of new fixtures since the time when the store fixtures being valued were bought. Such price changes may make the old fixtures either more or less valuable. If automobiles or delivery trucks are bought, they may be valued according to their condition. Valuations published in the used car and truck market reports furnish a good indication of average values.

In buying both fixtures and trucks, the prospective owner should determine if there are liens or mortgages against them. The seller should be asked for an affidavit that there are no claims against the fixtures and equipment. In addition, the public records in the county recorder's office may be examined to determine if there are any existing liens. If payments are still due on fixtures and equipment, the prospective owner should ask for receipts for the last payments. He should determine just what payments are yet to be made and who is to make them.

Buying goodwill. Goodwill—the name, the location, or the established clientele of the store—is sometimes a valuable asset. When buying the name and goodwill of a store, it is often stipulated in the contract that the seller will not engage in a similar business in the community for a specified number of years. On the other hand, goodwill is so intangible and so hard to value, that it is commonly omitted from the assets.

When the seller asks a substantial amount for his goodwill, the buyer has the problem of determining its value. One way is to ascertain the amount by which the business profits have exceeded the normal return on the capital investment. It may be assumed that the business, after paying a reasonable salary to the owner, has had an average profit over the past five years of $5,000, and that the net worth of the business as shown on the balance sheet is $40,000. It may also be assumed that money subject to the risks and hazards of investment in a mercantile

venture should earn 10 per cent. Ten per cent of $40,000 is $4,000; and, as the business has been earning $5,000, it may be assumed that $1,000 is the profit arising from goodwill. One thousand dollars capitalized at 10 per cent is $10,000, the estimated goodwill of this store. It is probable that this extra $1,000 profit results more from the good management practices of the owner than from the goodwill. If a new owner takes over, he has no assurance that his profit will be $5,000 a year. If he does not manage the store as efficiently as the former owner, it may be considerably less. Although the store may have some valuable goodwill, it is doubtful if this asset is worth $10,000. Frequently the actual amount must be determined by bargaining.

Another way of looking at goodwill is to consider it the difference between a reasonable valuation of the tangible assets to be purchased and the price asked by the owner. In the above illustration, if it is decided that the stock, equipment, fixtures, accounts, and buildings are actually worth $40,000 and the seller asks $45,000 for the business, the difference of $5,000 is the amount asked for goodwill.

Legal advice. When buying a business, legal advice should be sought before the transaction is completed. It is an advantage to both buyer and seller to have a lawyer draw the agreement and make sure that it is clearly understood by both parties.

All States and the District of Columbia have "bulk" sales laws to protect creditors in the event that a business is sold. These laws require that proper notice of the sale of the business be given to all creditors. If these laws are not complied with, creditors may claim the assets which the buyer has purchased. A lawyer will protect both parties by making sure that the transaction conforms to all legal requirements.

The lawyer will also give advice relative to the mortgages, liens, and other encumbrances which may be held against the assets, and arrange either for payments or transfer (of title) to the new owner. If payment for the business is not made in cash and there is a balance still due the former owner, the lawyer can draw the notes and mortgages which are necessary to put the agreement in effect.

Liabilities must also be considered when an established business is bought. Generally, it is not advisable for a new owner to assume the liabilities. It is desirable that the seller pay the debts which he has incurred. The buyer's attorney will determine if this has been done before the money for the business is paid to the seller. However, if the creditors are willing to accept a transfer of their claims, and the liabilities are assumed by the buyer, only the difference between the agreed-upon value of the assets and the assumed liabilities will be paid. This arrangement has a possible advantage for the buyer in that it reduces the net amount of cash which he must pay for the business and does not absorb such a large portion of his capital.

Buying into a partnership. An individual may become a partner in a going business (1) when one of the partners wishes to sell out; (2) when a new partner is needed to supply additional capital for expansion; or (3) when a new man is needed to provide additional managerial skill. Very frequently an employee buys an interest in the business for which he works. This is one of the most common ways of getting started as the part owner of a business. Perhaps one partner desires to retire and sells his interest to an employee. Perhaps a store is a sole proprietorship and the owner needs additional capital for expansion, or wants to be relieved of some of the responsibility of management, or wants to make sure a valued employee will not leave the business. Frequently an efficient man first becomes a partner in a store and later buys out the former owner and becomes the sole proprietor. The employee who buys into the business for which he has worked for years usually knows the value of that business and understands the man or men with whom he will share liabilities and responsibilities.

Before an outsider buys into a partnership he should consider arefully both the advantages and disadvantages of a partnership and the various methods of valuing the business. If his prospective partner or partners are capable men and if the business is fairly valued, buying a share in a partnership may be a good way of getting started in a retail business. It requires less capital than to buy or start a new store.

In a partnership profits and losses may be shared equally or

in such other proportions as may be agreed upon. All partners, except under very special circumstances, are individually responsible for the debts of the partnership and all their wealth, whether or not invested in the business, may be taken to pay the debts of the partnership. This means that one partner by mismanagement or dishonesty can incur debts which the other partner is obligated to pay even though it takes his home and all his other property. For example, if one partner sells the accounts receivable, signs notes at the bank, takes the cash and absconds, the other partner is liable for the debts of the partnership.

It is obvious that an individual should exercise very careful judgment before entering into a partnership.

Questions

1. What are the qualifications for the successful ownership and operation of a store?
2. What is managerial ability?
3. Upon what factors does the amount of capital required to operate a store depend?
4. On what scale can a retailer with $5,000 capital operate?
5. Where may a beginning retailer obtain capital?
6. What are the advantages of buying an established store? The disadvantages?
7. How should the value of the inventory be determined? The receivables? The fixtures? The goodwill?
8. Of what aid is a lawyer in the purchase of a retail business?
9. Should the buyer of a retail business ever assume the liabilities of the seller of the business? If so, under what conditions?
10. What are the advantages of buying into a partnership?
11. What are the disadvantages of being a member of a partnership?

17

The Importance of Store Location

LOCATION IS one of the more important factors determining the success or failure of a retail store. Many stores fail because of poor locations. The prospective retailer should select his location carefully, whether he buys an existing store or starts a new one. The prospective retailer may decide what type of store he wants to operate—based on his experience, ability, and personal preferences—and then find a good location for this type of store. Or, he may find a promising location and then operate the type of store suited to the location.

First comes the section of the country. Some prefer one part of the country and not another; some prefer a large city, and others a small town. A person from the South might be unhappy in a large industrial city in the North. One from the East may not like the Middle West. One may prefer to stay in his home town and if so, he analyzes the town and its trade area to determine what types of stores it will support. Or, if he has a definite kind of store in mind he searches for a good location for this type of store.

Many have no preference for any section or town; instead, they search for a good area in which to locate a particular kind of store. They may decide on an area that is developing rapidly and is not oversupplied with the kind of store under consideration. Many shifts in population have resulted from World War II, towns have grown, and new suburbs have developed. Some of these present good opportunities for opening new stores.

A man in Florida decided that he wanted to operate a hardware store. He looked over the figures and found that more hardware was sold in the agricultural Middle West than in any other section. He found a hardware store for sale in a growing town in the center of the Cornbelt. In this particular instance his choice was a wise one. However, one should not conclude that the best opportunities are always in the areas where sales are largest. Such areas may already have an adequate number of stores. All hardware is not sold in the Middle West and many successful hardware stores are found in other parts of the country. One may conclude that most gasoline is sold on main highways and that he should locate his station on such a highway. There may already be enough stations, however, on the highways while good opportunities exist in neighborhood locations off the main highways.

The type of goods to be sold affects the choice of a location. A good location for one type of store is often a poor location for another type.

Selecting the Town

There are two main problems in selecting the location for a store: first, the choice of the town or city itself, and second, the choice of a specific location in the town. Real estate managers of some chains believe that the selection of the town is more important than the selection of the location in the town, for no matter how good the location, the store will fail if the trading area does not provide enough business to support it. In the selection of a town, one should consider not only the town itself but also its trading area. A trading area is the territory in which live most of the people who come to a specific town to trade. The trading area varies for different types of goods. A large town or trading center usually has a much larger trade area for fashion goods than for convenience goods. A village may be a good location for a grocery store, a hardware store, or a filling station and yet a very poor location for a men's clothing store or a dress shop.

The retailer who intends to sell fashion goods should deter-

mine the trading area of the town he is considering. This can be done by studying a highway map and the population of nearby competing towns. Larger towns attract trade from greater distances than small towns. By considering the populations of the towns involved and the distances between them, the merchant may approximate the size of the trading area of the town involved. If undecided, he may write down the auto license numbers of cars parked in his town and then on a map plot the location of their owners from registration records. Or, he may ask people who live near the estimated edges of the area where they purchase the type of goods he intends to sell.

Population per store. When the boundaries of the trade area are ascertained, the area is analyzed to determine its desirability for the type of store contemplated. The first factor to be determined is the population of the area. Are there enough people to support the store? The following figures show the approximate number of persons per store in the United States in 1940:

	APPROXIMATE NUMBER OF PERSONS PER STORE
Grocery	340
Filling Station	545
Drug	2,280
Automobile	3,900
Hardware	4,500
Women's ready-to-wear	5,200
Building materials	5,280
Men's clothing	6,140
Furniture	6,600
Jewelry	9,100
Department	33,000

Several factors should be remembered in interpreting these figures. They are averages applying to all territories—those which consume many goods and those which buy few goods. For example, there was one building material retailer to every 5,280 people. In a built-up section of a large city where there is little new construction going on and where most of the building is usually done by large contractors who buy from wholesale dealers, it would take many times more than 5,280 people to support a building supply retailer. However, in a farming

and small-town community, fewer people may support such a dealer.

Another illustration: there is an average of 4,500 persons for each hardware store but in many large cities the number is over 6,000 and in many southern territories over 8,000. On the other hand, in many middle western counties the number is around 3,000 and in some counties that are almost entirely rural there are less than 1,000 persons per hardware store.

After allowance is made for regional and town-size differences, one may find areas where sales are low. This suggests an opportunity for another store. However, the people in this area may be accustomed to buying their goods in another type of store. For example, per capita sales of shoe stores may be low but the people may buy many of their shoes in department or general stores. Thus sale of goods in other types of stores should be checked.

Some chains have more or less definite rules about the population required to support a store of the type they operate. One drug chain does not open stores in towns of under 25,000, while a chain selling quality shoes wants 50,000 people in the trading area before it opens a store. Large variety chains seldom have stores in towns of less than 7,500 people. Yet there are dozens of small chains which operate stores in smaller towns. They often stay out of larger towns in order to avoid direct competition with the big chains.

Income. After studying the population, the prospective retailer should examine the income of a trade area. People with small incomes are poor prospects for many types of goods because low income families must spend most of their money for food, work clothes, fuel, and the like. There are several ways of sizing up the income of a territory. One way is the volume of retail sales. Another is to drive around and see what type of homes the people live in and what type of cars they drive. In a farming community, one should note the quality of the soil and the farm buildings. Another method is to note the quality of goods sold in local stores and the way people on the streets are dressed.

The size of the income of an area may be computed from

Census figures on rents and value of farm products sold.[1] Many other figures are used to indicate the relative prosperity of an area: bank deposits, postal receipts, automobile registration, number of income tax returns, real estate values, and circulation of leading magazines. Many of these figures can be found in *The Consumer Market Data Handbook,* published by the U. S. Department of Commerce. *Sales Management* magazine publishes annually an estimate of the effective buying income in all counties and cities in the United States.

Other factors. Many other factors should be considered. The demand for some types of goods varies with the type of farming, the prevailing racial stock, the climate, kind of fuel used, the hardness of water and its source, sports available, religion, and the like.

The prospective merchant may call on representative consumers and ask them if the stores in the community serve all their needs, if they are unable to get some kinds of goods locally, and the type of goods they prefer for various uses. Much valuable information can be obtained in this way and at the same time goodwill can be built.

Selecting the Specific Location

Once the town is selected, the prospective retailer must select a specific location in the town. A good location is so important that a chain store company may wait several years in order to obtain the specific building it wants. Chains often refuse to place a store in a town until they can secure a desirable location.

The retailer should know the factors determining the value of a location. A desirable location varies with the type of goods sold and the kind of store operated. We speak of the "100-percent location," meaning the spot having the largest number of

[1] Housing Census for 1940, Vol. I, Part I, table 5 shows rent for all non-farm homes. By multiplying the monthly rent by 12 and this by the number of non-farm families we get the total annual rent. This may be capitalized to get the non-farm income of the area. The figure used in capitalizing rent varies from perhaps 8 per cent or less in rural areas in the South up to 20 per cent in large cities in the North. Farm income must be added to obtain the total income of an area. Farm income can be found in the Agricultural Census, Vol. II, Part I showing value of products sold, traded, and used.

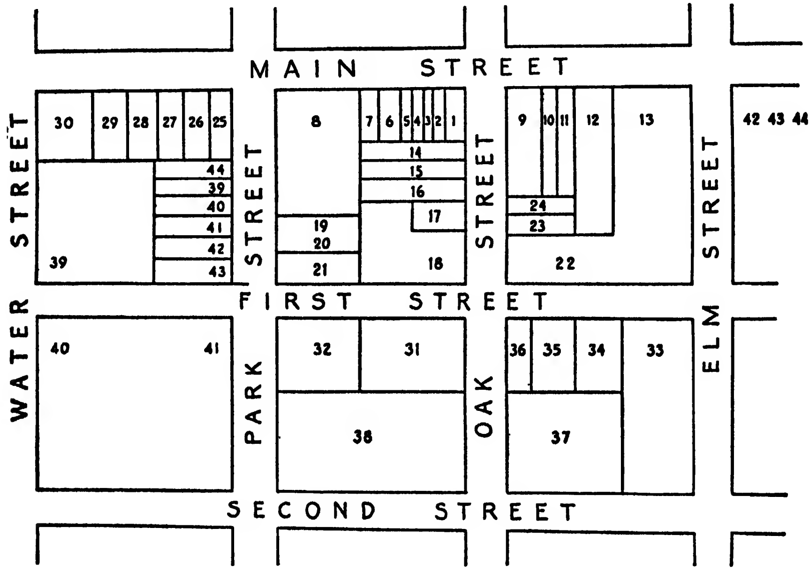
pedestrians passing (the heaviest sidewalk traffic), although at times we use the term in referring to the best location for specific kinds of stores.

In the accompanying diagram, No. 1 indicates the 100-percent location. The block between Oak and Park streets is the 100-percent block. The block between Oak and Elm is the second best block with only slightly lighter traffic. The block between Park and Water and the opposite side of Main Street has considerably lighter traffic. By counting the passers-by for several short periods, we secure totals. The higher number is taken as 100 per cent and the other locations rated as percentages of it. In the diagram, No. 1 is 100 and the others may be as follows: No. 5, 80; No. 8, 90; No. 25, 40; No. 9, 90; No. 12, 50; and so on. This diagram represents a rather common pattern found in retail shopping districts and might be that of a city of from 10,000 to 250,000, or an outlying retail district in a larger city. A town of 5,000 will have fewer stores on side streets; a larger city will, of course, have a larger retail district.

In the 100-percent location are usually found drug, variety, or department stores with clothing, shoe, dress, millinery, and hosiery stores nearby. Drug and variety stores sell principally convenience goods and want to place their stores where they are easily accessible to a large number of consumers. Department, clothing, and millinery stores sell fashion goods and want to be in the center of the shopping district.

It may be assumed that No. 1 in the diagram is a drugstore. Locations 2 and 5 may be dress shops, shoe stores and millinery stores. Numbers 6 and 9 may be variety stores and Numbers 8 and 13, department stores. Furniture is a fashion good, but, as it is more bulky, furniture stores are often located at the edges of the main shopping district. In the diagram, locations 18 and 30 might be furniture stores. The other locations on both sides of Main Street between Elm and Water Streets will house men's clothing, drug, luggage, dry goods, confectionery, shoe, jewelry, stationery, and household appliance stores, as well as banks, restaurants, and hotels. Hardware stores are usually on the edge of the shopping section, perhaps in locations 39 and 42. Automobile sales rooms and garages are usually on secondary

streets or on main streets outside the shopping district. In the diagram they might be 37 and 41. Parking lot stores (like supermarkets) are usually located outside but near the shopping district, perhaps in locations 32, 38 and 40. Filling stations are usually located on main arterial streets outside the shopping districts. In small towns, they are often on Main Street at the ends of the main business block or blocks.



Typical Retail Shopping District

This outline gives a general idea of the kind of location which should be selected for various types of stores. There are, however, several other factors to consider. The retailer may pay a high rent to get in a location with heavy traffic and depend largely on window displays to attract customers to his store. Again, a small store may find it advisable to locate in or near the 100-percent block while a large store may locate a block or two away and depend upon its size and prestige to attract customers. This is often done by popular-priced department stores and occasionally by large variety stores. At times the retailers believe landlords are charging too much rent, and a few of the medium-sized stores (variety, drug and apparel, for example) go

together and move a block or two from the 100-percent block, either along Main Street or on a cross street. In some cases this is very successful and causes a shift in pedestrian traffic and real estate values. A popular-priced chain of department stores may take an "off" location (for example, Number 22 or 33 in the diagram) and depend upon its reputation and prices to attract customers. Or, it may locate on Main Street near the 100-percent corner. Decisions appear to be based on availability of buildings and the amount of the rent.

A "merchandising" store appealing principally to transient trade should be in a heavy traffic location while a service store with an established reputation for high quality goods may prefer a less costly location.

Retail districts move. The 100-percent location today may be a 60-percent location in ten years. The retailer looking for a location should try to locate ahead of and in the path of the movement. In the diagram, Main Street runs east and west and the railroad station is to the east. The business section started at the railroad and grew west. If the retail district is still moving west, the newcomer may do well to rent between Park and Water streets rather than between Elm and Oak; there is less traffic and rents will be lower, but the location promises to increase in value. If he goes farther from the center of the district, he may do better to locate west of Water Street rather than east of Elm.

Parking facilities are important. Many grocery stores have left the center of retail districts because of limited parking space. Other types of stores may find it profitable to locate a little distance away from the center if the proposed location provides space for customer parking.

Traffic counts. The traffic passing various locations may be determined by making several counts for short periods of perhaps five or ten minutes. Counts should be made on various days, in various kinds of weather, at various hours of the day. Counts should be tabulated separately for men and women. Often one side of the street is the women's side. The north side may have much lighter traffic but may have almost as many

men passing as the south side. If so, it may be a good location for a men's clothing store if the rents are lower than on the south side of the street.

The apparent destination of people passing should also be noted. People going to and from work, or going to railroad or bus stations, may be poor prospects for most types of stores. One may be easily misled by traffic counts unless allowance is made for this factor.

The reason for having a location with many passers-by is to attract many customers into the store. The number of people entering a store depends upon the number and type of people passing, the window displays, the type of merchandise handled, the store's prices, and the size and reputation of the store. To illustrate: two stores with similar frontages selling similar goods and located in the same town had the following number of passers-by during the period counted: A, 1,930 and B, 2,700. Store A was located near a bank and many of the passers-by were going to and from the bank and were not shoppers, while most of those passing store B were shoppers. Eleven per cent of those passing A entered compared with 4 per cent of those who passed store B. Thus in a given period A had 212 customers and B had 108 customers. The reason is that A has better windows and a much larger stock of goods. As a general rule, a store on a street with a high traffic density will attract a lower percentage of the passers-by than will a store on a side street because many of the people on the side street come there to enter the store.

Actual traffic counts in towns of various sizes show the following variations in the percentage of passers-by who enter: hardware, from 3 to 40 per cent; drug, from less than 2 to 37 per cent (most stores in the sample 10 to 16 per cent); variety chain stores, from 18 to 52 per cent (most stores in the sample between 20 and 30 per cent); and department stores, from 14 to 43 per cent.

Some variety and drug chains can predict with a high degree of accuracy the percentage of passers-by who will enter a store of a certain frontage which has standardized window displays. The beginning retailer has no such experience. He can, how-

ever, make traffic counts of stores that are similar to the one he expects to operate and similarly situated. This will indicate the proportion of passers-by who will enter his store once it has established a reputation.

If he knows the amount of the average purchase, he can then compute his expected sales. Let us assume that the average sale in his type of store is $1. A store on a street with 10,000 people passing per day and attracting 8 per cent of them would expect daily sales of $800. On a side street with 1,000 people passing he might attract 20 per cent and have daily sales of $200.

Neighborhood locations. The prospective retailer often has the option of locating in the central retail district, or in an outlying or suburban district. In large cities most stores selling convenience goods such as groceries, drugs, household hardware, and prepared foods are located outside the central shopping district. As outlying retail districts grow, fashion goods stores come in until, in our larger cities, many large fashion goods stores are found in outlying retail districts.

Rent may be lower in a neighborhood location. The retailer can live nearer his business. He can get acquainted with more of his customers and has the opportunity to "personalize" his store. If he can select a neighborhood or suburb that is growing and is not oversupplied with stores, he may do well to locate there. Zoning laws should be examined to ascertain if the building can be enlarged if expansion becomes necessary.

Highway locations. Some stores locate outside towns on main highways. This location is frequently selected for filling stations, restaurants, and fruit stands. Stores selling fashion goods such as furniture and clothing sometimes select highway locations. Highway stores are usually open evenings and appeal to people who want to take an after-dinner drive. They allow husband and wife to shop together. They have ample parking space. In spite of these advantages the inexperienced merchant should investigate carefully before choosing such a location.

Building. In selecting a location it is important to secure a building suited to the store. Does it have proper display windows? Is the floor suitable for the type of goods handled? Is the ceiling high enough or too high? Are there posts in the

store room? Does it need new lighting fixtures? Is there a rear or side door for the receipt of goods or will they have to be brought in the front door? Is there storage and office space? Does it have the necessary toilet facilities? If more than one floor is to be used, does it have proper stairs or an elevator? If it has to be remodeled, who will do it—the owner or tenant? If the latter, how much will it cost? Does the building comply with local fire and sanitary ordinances? What insurance rate will it take? Is the building a "fire trap" or is it located in an area with high insurance rates?

Buying versus Renting

Once a suitable location is found, the prospective retailer must decide whether to buy or rent. Most stores are operated in rented buildings but at times property must be purchased to get the desired location.

At other times, a retailer must erect a new building to secure one suited to his needs. In either case, if he does not want to retain ownership he may sell it and keep a long-term lease with rentals that make the building a good investment. Most beginners do not have sufficient capital to enable them to purchase buildings. Those who do should consider the step carefully. Real estate values change. A given location may increase or decrease in value with the passing of the years. If the retailer owns the location, he benefits from an increase in value. He gets more customers without paying more rent or he can sell the building and take a profit. On the other hand, if the value of the location decreases, the owner takes the loss. The retailer should consider the trend of values in the district with special care before he buys.

Typical rents. Typical rents in the 1930's are given on the next page.

During periods of rising prices the percentage cost of rent usually decreases. During the War and readjustment period, for example, some chains of department stores used 2.5 per cent as the maximum allowable cost of rent.

It will be noted in the table below that stores selling con-

venience goods usually had lower expenses for rent than stores selling fashion goods. Exceptions were garages and restaurants, which use considerable amounts of labor in repairing cars and cooking and serving foods, and paint and drug stores. The latter have many small sales and often find it desirable to be located in high rent districts. Most of the stores selling fashion goods had rent expense of 3.1 to 5.2 per cent.

TYPE OF STORE	PERCENTAGE RENT EXPENSE*
Grocery	1.9
Grocery and Meat	1.4
Country General	1.3
Farm Implements	0.9
Feed	0.9
Building Materials	0.7
Automobile	0.9
Coal	1.0
Hardware	3.0
Hardware and Implements	1.6
Filling Stations	2.7
Electrical and Household Appliances	2.0
Drug	3.3
Restaurants	3.6
Paint, Wallpaper, etc.	4.2
Garages	4.0
Auto Accessory	2.8
Dry Goods	3.1
Variety	3.8
Men's Clothing	3.2
Men's Furnishings	4.0
Women's Ready-to-wear	4.4
Shoe	4.5
Millinery	8.4
Jewelry	5.2
Furniture	3.8
Radio	4.1
Florists	5.2
Books	5.0
Family Clothing	3.2
Department	4.2

* Most of these figures from Dun & Bradstreet.

The percentage of sales spent for rent usually increases with an increase in the size of the town as illustrated by the following figures for stores with annual sales of between $30,000 and $50,000:

TYPE OF STORE	SIZE OF TOWN	PERCENTAGE RENT EXPENSE
Grocery and Meat	Under 20,000	1.2
	20,000–99,999	1.4
	100,000 and over	1.6
Restaurants	Under 20,000	2.3
	20,000–99,999	4.5
	100,000 and over	4.6
Shoe	Under 20,000	3.8
	20,000–99,999	4.4
	100,000 and over	6.5

The figures in the two foregoing tables are averages. The retailer as a rule desires to pay somewhat below the average unless he secures a good location where the volume of sales or the prices he can charge make his business profitable at the higher rent.

Flat or percentage leases. Leases are of two kinds: flat and percentage. Under the flat lease, the dealer agrees to pay a fixed amount of rent each month. Under the percentage lease he agrees to pay a given percentage of his sales.

With the percentage lease the merchant does not pay high rents in poor years. In some instances stores have been burdened, and even forced into bankruptcy, in poor years by leases with flat rentals signed at high rates in periods of good business. Some leases signed during the 1920's became very burdensome during the 1930's. Percentage leases guard against this disadvantage. It is said that a percentage lease is fair as the landlord gets just what his location is worth and nothing more. On the other side, the dealer pays just what the location is worth—no more, no less. The percentage lease is especially practical for a new dealer who does not know what his sales will be.

Percentage leases frequently specify a guaranteed rent plus a percentage of all sales above a fixed amount. For example, the lease may call for a rent of $100 a month with 4 per cent of all sales over $30,000 a year. If the dealer ordinarily has sales of $50,000 to $60,000 a year, he may be protected against paying a high rent in a poor year. If, however, his sales are normally $30,000, they will probably drop below $30,000 in a

poor year so that the percentage lease will not protect him against an excessive rent. When the dealer signs a percentage lease, it is very important that he make sure that the guaranteed rent is not too high.

Another advantage of the percentage lease is that a long-term lease can be signed with less risk to both owner and dealer than is possible with a flat-rate lease. The value of a location may increase or decrease greatly during the life of a long-term lease. With a long-term flat-rental lease, the dealer gains if the location improves and suffers if it declines in value.

The disadvantage of the percentage lease is that if sales increase, the dealer must pay more rent. The increase in sales may be the result of good merchandising on the part of the dealer and not of increased traffic passing the store. To pay more rent under this situation means that the landlord shares the profits resulting from the dealer's efficiency. This seems unfair. However, if the dealer builds a good business, he has increased the value of the location, and under a flat-rate lease it is very probable that the landlord will increase the rent when the lease expires. The dealer must then pay the higher rent or go to all the expense of moving and probably losing some of his customers as well. Dealers who oppose percentage leases say they prefer to set aside reserves in good years to cover losses during poor years.

In the long run, flat and percentage leases are said to work out so that tenants pay approximately the same rent. Although this may be generally true, in individual cases the dealer may be either much better or much worse off because of such a lease. There is a great deal of negotiation or higgling in arriving at terms. Too often neither the tenant nor the landlord knows the exact value of the location for a given type of business. The more information the tenant has as to how much business he can reasonably expect to do in a given location, the better position he is in to negotiate a favorable lease.

Leases contain many kinds of provisions. In some cases the tenant pays part or all of the cost of alterations, repairs, insurance, or taxes. The percentage he pays may be on a sliding scale and either decrease or perhaps increase with increased

sales. In the lease above the dealer might pay 4 per cent on sales between $30,000 and $40,000; 3½ per cent on sales between $40,000 and $50,000; and 3 per cent on all sales over $50,000. The terms of the lease should be clear. How long is the lease to run? Under what conditions, if any, can it be renewed? Are there any restrictions on the use of the building? Can the tenant sublet a part of it? Who is to make repairs to the building? Does the tenant have the privilege of putting in a new front? If so, is the cost to be divided or is all of it to be borne by the tenant?

Questions

1. How may the type of goods have a bearing on where a store is located? Illustrate.
2. What are the two main problems in selecting a store?
3. If the population for a particular kind of store is high in a given trading area or town, does this fact mean that it is a good place in which to locate the store?
4. How may the income of a trading area be determined?
5. What other factors should be considered in selecting a town in which to locate?
6. What is meant by the term "100-percent location"?
7. What factors should be considered in selecting the particular side on which to locate?
8. What should be considered in selecting a building in which to locate?
9. Should the retailer buy or rent his store building?
10. What are the two kinds of leases?
11. What are the advantages of a percentage lease? The disadvantages?
12. What are some of the provisions which a store lease should contain?

18

Selecting, Training, and Supervising Employees

ALL BUT small family-operated stores must hire one or more employees. The small store may hire a new employee only infrequently while the large store needs many employees. The proprietor of a small store may need only a salesman and perhaps a part-time bookkeeper. The large store may need several salesmen, one or more repairmen, one or more bookkeepers, a delivery man or two, and perhaps a credit manager, a cashier, and a porter.

Job Analyses

One of the fundamentals in hiring workers is to have clearly in mind what their duties are so that persons with qualifications for performing these duties can be employed. The following outline indicates briefly the duties or work required in the operation of a store:

Buying:
- Ordering goods (from data secured from want lists, check lists, inspection of stock, inventories, or stock records).
- Purchasing: Selecting sources of supply, negotiating contracts, buying job lots, goods for specials, etc.
- Interviewing salesmen.
- Trips to market to locate goods.

Selling:
- Waiting on customers.
- Handling telephone orders.
- Outside selling, including finding prospects.
- Selling by repairmen when in homes of consumers.

Advertising:

Selecting goods to advertise.
Writing copy for newspapers, direct mail, handbills.
Securing mailing lists.
Addressing direct-mail advertisements or supplying mailing lists to the agency that sends them out.
Arranging store and window displays.
Writing store and window signs.
Negotiating contracts with newspapers, printers, jobbers, or others selling advertising materials.

Clerical (often performed by salespeople):

Wrapping packages.
Totaling orders and adding taxes.
Making records of sales.
Making change.
Checking credit on charge sales.
Filling out want slips (goods out of stock or not handled).
Marking prices.

Stockkeeping:

Checking in orders.
Placing goods in reserve stocks.
Replenishing stocks on sales floors.
Taking inventories.
Keeping stock clean and displays in order.

Accounting:

Keeping books.
Preparing government reports.

Credit:

Passing on applications for credit.
Making out and addressing statements.
Making collections.
Cashing checks.

Delivering:

Making deliveries.
Handling c.o.d. orders.
Handling returned goods.
Care and upkeep of truck.
Arranging for delivery by an outside delivery company.

Janitor service:

Sweeping and cleaning store, stockroom, and sidewalk.
Washing windows.
Cleaning and changing lights.
Tending heating equipment.

In a small store, the proprietor will probably do all or most of the buying, all or most of the advertising work, all or most of the credit work, and some of the selling, clerical work, and stockkeeping. Salespeople do much of the selling, clerical work, stockkeeping, and in smaller stores they may spend part of their time in other work such as delivering, repairing, or janitor work. Larger stores have special workers to keep books, handle credits, make repairs and deliveries, and clean up the store. Keeping clearly in mind the duties which he wants an employee to perform will help a retailer in hiring persons suited to these duties.

How to Obtain Employees

Applicants for positions may come in voluntarily or the retailer may locate employees by advertising in the want ad section of local papers, by placing signs in his windows, by contacting local schools, or by having his employees suggest possible employees.

Applicants who come to the store voluntarily are supposedly particularly interested in the kind of merchandise the store handles. On the other hand, they may simply want any job and try all the stores along the street until an opening is found. Signs placed in the store window or ads run in local papers are used very frequently. One way of securing applicants is to contact the local schools. The high school principal or personnel counselor often can select persons who are interested in retail work and who have the desired qualifications. High schools and business colleges are usually good sources for bookkeepers, stenographers, and cashiers. Sometimes the retailer may contact colleges and universities. This is likely to be true when a department or store manager, an accountant, advertising manager, or credit manager is wanted.

Retail establishments sometimes prefer to employ people who have attended a college one or two years but who have not graduated. These men and women have more training than high school graduates and are somewhat older. They believe

that such employees are more likely to be permanent than are college graduates because the latter, wanting more highly paid work, may not remain with the store.

Some retailers believe that persons suggested by employees are especially desirable. Such workers are likely to know something about the store and the work from their friends who work in the store. An employee, however, in trying to help a friend or relative may recommend an individual who may not be a particularly good worker.

Qualifications of Employees

The qualifications needed by employees may be outlined briefly.

Salesmen. Salesmen should know the merchandise and how to handle people. They should like people and know the principles of salesmanship. They should know how to greet customers, ascertain their wants, present the goods, furnish the customer with information about the goods, make suggestions and close the sale.

Retail salespeople should have sufficient education and culture to keep themselves and their clothing neat, to use good grammar, to talk intelligently about the goods, and to treat the customers tactfully. If persons with too much ability are employed, they may graduate into better positions and give the store the problem of constantly training new workers. Some retailers prefer to employ people of average ability in order to secure more permanent employees and thus reduce their rate of employee turnover. Others prefer to employ salesmen of outstanding ability in order to secure superior salesmen even though new ones must be employed from time to time to replace those who leave to start their own stores, to manage stores for others, or to become wholesale salesmen.

Retail salespeople have to be on their feet most of the time. Persons who are unusually stout are apt to tire easily and are therefore not preferred for such positions. Persons somewhat taller than average height are often preferred for selling. How-

ever, neither physical characteristics nor age are of fundamental importance. Personal character traits are more important.

Previous selling experience is preferred by some employers. An applicant with selling experience has less to learn, can be put to work immediately, and taught the prices, store system, and stock arrangement quickly. If he was successful in his previous job, it may be difficult to adjust the new employee to the policies of his new employer. If his former employer was careless in handling customers and in keeping stock, the salesman may have become careless and it may be hard to change him. For this reason some retailers prefer to train their own employees.

Then there is the question of why the employee wants to change jobs. If the other store is closing, the reason may be obvious; otherwise the man may have been unsatisfactory, and the new employer should examine the man and his record carefully. It is usually considered unethical for an employer to approach the employee of a competing store. However, if the employee makes the contact it is ethical to consider his application.

The situation is slightly different when the applicant has had retail selling experience in another type of store. He may know little about the particular kind of merchandise which the store handles, but he does know how to handle customers, make out sales slips, and perform various duties required of a salesman. He only needs to obtain a knowledge of the merchandise. There is much in favor of employing such people. While the new employee is learning about the merchandise, the dealer may also explain the store's policies and practices in handling customers, keeping records, extending credit, and the like.

Bookkeepers. Relatively little knowledge is required to keep simple books according to instructions. If a system is to be devised to suit the individual needs of the store, however, a very competent individual should be employed.

Credit men and advertising managers should have the necessary training and experience fitting them for their highly specialized work. The knowledge and abilities required for these positions will be presented later.

How to Select Employees

In selecting new employees, the retailer should interview the applicants, consult their references, and verify their statements about previous experience. He should also remember that the abilities of different people vary greatly. Two men of the same general appearance may possess similar backgrounds of education and experience, and yet one will have more ability and a greater aptitude for retailing than the other. The retailer who can choose superior employees and then stimulate them to do their work will in all probability be an outstanding success.

The interview. The interview consists of two parts: the size-up, and securing information from the applicant.

The size-up. Experienced personnel managers depend somewhat on their size-up of applicants. They base their judgment on the appearance of the applicant's clothing, his bearing, facial expression, and greeting. His clothes need not be expensive, but they should be clean and in good taste. A very successful retailer says that his success has been due largely to the men he has selected to work with him. He judges people by their carriage and by their manner.

The way in which the applicant greets the interviewer indicates much as to his self-confidence and his ability to talk to customers. Many successful men, however, were awkward, scared, and more or less tongue-tied when they applied for their first jobs. Evidently there is more to employee selection than the superficial appearance of the applicant. Information must be secured by talking with the applicant.

Information. One main purpose of the interview is to find out about the applicant's education, experience, the environment in which he grew up, and his desires and ambitions. Another purpose is to tell the applicant about the job: what it involves, the pay, the opportunities for advancement, and privileges such as vacations with pay, discounts on purchases in the store, pension plans, and other things concerning the job or store.

Specific facts obtained from the applicant may include the

following: age; place of birth; nationality; occupation of father; religion; where reared (on farm, in village, or in a city); family life; education; experience of all kinds; hobbies and interests; health; use of intoxicants; community, social, political, and religious activities; and references. The interviewer should have definite reasons for obtaining each specific kind of information. Previous work experience is especially important. Hobbies and interests may be of some value. A person who is active in community and social affairs is usually one who likes people and gets along well with them, who makes friends, and who may be expected to attract a certain amount of trade to the store. It is easy, however, to over-estimate the importance of such activities.

Perhaps the most important questions to ask applicants are: "Why do you want to work in my store?" "Why do you think you can sell our merchandise?" The answers to these questions may show whether the applicant is truly interested in retailing or whether he is just looking for a job. They also may throw much light on the applicant's general attitude. The latter, as well as his determination to succeed are very important in anticipating his success in the job. Sometimes it is desirable to interview the applicant two or more times, to note what he says at the first interview, and see if he gives the same facts at the second interview.

References. Usually applicants are asked for references, who are then contacted personally, by letter, or by telephone. It is to be expected that the prospective employee will give the names of persons who will speak favorably of him; this fact should be remembered in evaluating the information obtained. References should, however, be used to verify facts as to previous employment and education, and to provide a general rating of the applicant's ability.

The difficulty in the use of references is that some individuals will say a good word for anybody. Occasionally an employer who wants to be rid of an employee may give him a high rating to induce someone else to hire him. Unless the retailer knows the reference personally and knows whether or not the reference is liberal or conservative in his judgments, not too much importance should be attached to any one reference.

The retailer also may consult persons who know the applicant but who were not given as references. These individuals are apt to be more frank in their comments than the persons who have been listed. The applicant's educational attainments may be obtained from the schools. His grades, attendance records, and attitudes sometimes furnish valuable clues to his abilities and ambitions.

Training Employees

The training of retail store employees may be divided into three parts:

1. Training in store policies, store organization, conduct of employees, handling customers, and store system.
2. Knowledge of goods and their uses.
3. Training for specific jobs and duties.

Employee training in store policy. The following outline of policies includes the kind of information that every employee should have regardless of his duties. The individual retailer may modify or enlarge on this outline to suit his particular organization.

1. Every employee is a personal contact between the store and the public, and his actions and attitude will influence the customers' opinion of the store.
    a. The first rule of conduct is courtesy and patience.
    b. The second rule is alertness in handling customers.
    c. Employees should never engage in arguments with customers.
    d. Employees should not raise their voices in the store nor argue with each other; they should coöperate fully with each other.
    e. An important objective in the independent store is to have employees know customers personally.
    f. Friendliness with customers does not mean familiarity.
    g. Telephone conversations should be handled with the same care and tact as personal conversations with customers.

2. Employees are expected to keep their persons clean, and their attire neat and presentable.

3. Punctuality is expected of all employees.

4. Employee complaints should be made direct to the proprietor.

5. Suggestions for improving the store methods, merchandise lines, store layout, or any other ideas for improving service are welcomed by the proprietor.

6. A "selling" attitude and atmosphere should prevail among employees, but no "high-pressure" selling tactics are to be used. Intelligent service is desired.

Some of the larger stores provide employee manuals and i_ may be advisable for the small store to develop one. The small retailer may find that preparing such a manual aids him in formulating his policies and practices on many matters: extending credit, cashing checks, making deliveries, holding goods on a deposit, making c.o.d. sales, store hours of employees, vacation rules, sick leaves, and the like.

The following will illustrate the contents of a manual:

No employee, other than the manager, has authority to pay out any money without the approval of the manager.

Salespeople are not to accept any checks on any bank without first having the manager's O.K. on the back of the check. No checks can be cashed and no checks accepted in amounts greater than the actual sale.

Customers' complaints regarding defective merchandise should be handled courteously. Where there is no question that the article is defective, make a replacement. No one but the manager has authority to pass on refunds. If taxes have been charged on the sale, be sure they are included in the refund. All refund slips must be signed by the customer.

All full-time employees will have the privilege of making personal purchases at 10% off the retail prices.

Mark-downs if not controlled are the source of large shrinkages and can seriously affect the profit of the store. Other than for special sales, mark-downs should be taken only because goods are broken or damaged; incomplete goods—as parts missing—or shopworn goods; and shelf-warmers or slow-moving articles. When goods go on sale, mark all items in stock with the new price with a different colored pencil. If any marked-down goods are not sold

during the sale, prepare mark-down cancellation tickets for the quantity left and put price back to normal.

Knowledge of goods. In a small store, the new salesman is usually trained by the proprietor and the older salesmen. After brief training in how to handle cash, make change, use cash register, make out sales slips, and handle credit sales, he is usually sent to the sales floor to watch the older salesmen work for a few days. He may then begin selling, although he must ask other salesmen for the location of certain merchandise, how it is used, and for information to give customers as to merchandise quality and care.

The new salesman should have his attention called to sources of information about the merchandise. New employees should be encouraged to study this material when there are no customers present or other work to be done.

One source of information available to the new employee is to ask the experienced customer how certain items of merchandise are to be used. Experienced customers may be glad to give this information. They may feel flattered that they are asked.

Training in specific duties. Specific training is necessary for several types of employees. If service and equipment maintenance men are hired, they will need training in store policies. They can find many sales prospects and do much to gain and keep customer goodwill when they visit homes to make appliance and machine repairs. These employees need instruction on stockkeeping for repair parts and on ordering of additional parts. They will need instruction on how to keep the shop clean, tools and parts in order, and to do this work when not actually making repairs or out on contract jobs.

Special training may also be advisable for office employees. Instructions usually include dates for mailing of statements, dates for second statements on unpaid bills, collection procedure for slow accounts, keeping of sales and stock records, classification of expenses, and the like.

The assignment of well-defined duties is an aid in training employees as well as in supervising their work. It is true even in a small store operated by the proprietor and one salesman.

In such a store the proprietor will probably do all the buying, and most of the advertising. He may trim the windows or he may be responsible for one and make the salesman responsible for the other. The proprietor may be responsible for keeping the stock in order and the shelves and drawers full on one side of the store while the salesman does the same for the other. Since the proprietor handles the buying and advertising problems, the salesman may be made responsible for keeping up the stock on the center tables. Each may check stock to prevent out-of-stock items, or they may take inventory together and check certain lines each week.

As the store expands, there is a greater need for each employee to be assigned certain definite duties. If the store is not departmentalized (salesmen assigned to definite departments), salesmen should wait on any customers who enter. When no customers are present, they can do stock work. Each salesman should know what stock he is responsible for keeping clean, in order, properly displayed, and checked against shortages. If he has other duties, such as helping address statements or advertisements, he can plan to attend to them when not needed on the sales floor.

Outside training courses. In many cities and towns evening courses in retail selling, retail store operation, retail advertising, bookkeeping, and credit are conducted by the Chamber of Commerce, and by high schools, colleges, universities, Y.M.C.A.'s, and business colleges. At times arrangements are made for employees to attend morning courses on store time. Instruction may vary all the way from a series of lectures to formal courses with text assignments, examinations, and credit given to those who desire it. Correspondence courses in retailing are particularly helpful for employees located in small towns where evening courses are not available. Employees should be encouraged to attend or enroll in courses related to their jobs.

Supervising Employees

One of management's problems is to select people who have the ability to perform their duties efficiently. A second goal of

good management is to lead and to stimulate people to do their best work. Superior leadership and supervision will obtain good results from people with only average ability.

Supervision is an art. Praise will, as a rule, win better results than criticism, yet most retailers are too sparing in their praise of employees. Some employees, of course, need constant prodding and reprimands. Employees should, if at all possible, be handled individually according to the method which will obtain the best results. Few employer actions will alienate the good-will of employees more quickly than unfairness, partiality, and failure to keep promises. Supervision involves a check on the performance of individual workers. Sales records will show the volume of sales per clerk. Inspection of the stock sections will show how clean and orderly each man keeps his stock. The presence or absence of customer complaints is also important. Some stores hire outside shoppers to observe their salespeople on the job.

A system of rewards is very important in stimulating employees to do their best work. Increases in wages or salary are the most welcome recognition for a job well done.

Methods of paying salespeople. There are several ways of paying retail salespeople: a straight salary; a straight commission; a straight salary with a commission on all sales over the salesman's quota; a flat wage with a bonus based on the store's profit or on the all-around performance of the salesman. Most retail salespeople are paid straight salaries, with perhaps the addition of PM's (special payments or bonuses) for the sale of slow-moving articles.

The straight salary is easy to compute, gives the employees an assured income, and is adapted to the small store where the salesmen sell a great variety of articles, some at low prices and some at high prices. The great disadvantage of the straight salary is that it offers no special incentive for the salesman to increase his sales. It may be that a salesman receives a salary raise when he increases his sales but the increase is usually slow and often not commensurate with his increased sales. However, the salesman on a straight salary does not have his salary reduced every time his sales fall off. The straight salary thus

protects the salesmen in times of poor business and protects the retailer when sales increase.

The straight commission is used infrequently in retail stores although it is sometimes used by stores selling furniture, clothing, automobiles, and large appliances. This method gives the salesman no guaranteed income but it does provide a strong incentive to sell. This often leads to high-pressure selling. Such selling is out of place in the store that wishes to keep customers coming back regularly.

A salary with a commission on all sales over a quota is better suited to retail salespeople than the straight salary. It gives the salesmen an incentive to increase their sales, if the established quota is not too high. If the quota is set so high that the salesmen do not expect to reach it, the method is almost the same in its operation as a straight salary. On the other hand, if quotas are set too low, the salesmen work for their commissions and the plan has the disadvantages of the straight commission plan. To stimulate the salesmen without encouraging high-pressure selling requires carefully adjusted quotas.

Quotas may be set annually, semi-annually, quarterly, or monthly. The actual quota may vary from one salesman to another. In a store where salesmen are assigned to definite departments, the quota will vary from one department to another. When quotas are set up for shorter periods, seasonal variations in sales should be considered. When quotas are set, they should not be increased without a good reason, and this means a reason that seems good to the salesman as well as to his employer.

One objection to paying salesmen on a salary plus commission basis is that they will neglect other duties such as keeping stock clean and goods properly displayed in an attempt to wait on as many customers as possible. If specific duties are assigned to each employee as suggested earlier, this objection will be largely overcome. If a salesman neglects the stock sections assigned to him, his negligence will be apparent. When a salary and commission method of paying salesmen is used, care should be taken to prevent high-pressure selling tactics.

Bonuses may be paid for reasons other than increased sales.

The employees may be given a share of the store's profits after the owner has been paid a specified salary plus the interest rate on his investment. Such a plan may include all the store's employees. It should stimulate them to increase sales, reduce waste, cut expenses, keep the store clean, and the stock well displayed. On the other hand, the store may lose money through no fault of the employees. The bonus based on a share of profits is so uncertain and so long delayed that it often fails to act as a strong incentive.

Bonuses may be based on the retailer's opinion of the employee's value and faithfulness in performing all his duties; selling, care of stock, keeping store clean, keeping records; making deliveries, making repairs, finding prospects, handling customers, preparing advertisements, taking stock and other duties.

Paying other employees. Employees other than salesmen are usually paid straight salaries, except those who can be paid on a piece-rate basis. Deliverymen may be paid so much per trip or per package for town deliveries; the method is less suitable for country deliveries, where distances vary greatly. Piece-rate payments are sometimes more practical for part-time than for full-time employees.

Other rewards. Other rewards may include vacations with pay, sick leave with pay, full or part payment on pension plans to secure larger retirement pay than those provided by federal law, and payment for suggestions. When such systems are started they are likely to prove excellent incentives for better work. After a few years, however, they are usually taken for granted and other methods of stimulating workers must be developed.

Building morale. Building morale is important in any organization. Good treatment of employees may include good working conditions in the store, reasonable hours of work, provision for recreation, and arranging parties or picnics for store employees and their families. Sometimes bowling, basketball, or other athletic teams are sponsored by the store for its employees. Larger stores may promote musical or dramatic programs and clubs. Although the small store cannot use as many of these ideas as can the large store, the proprietor's personal

interest in his employees and their welfare should prove even more successful.

Watching sales cost. When expenses are above the average for similar stores the retailer should study his operations and find the cause. Often a salesman's salary is advanced as his sales increase. Later, owing to poor business conditions or to a decrease in his effort, his sales decline. This results in a higher percentage of sales operating cost. In other cases it may be necessary to raise employees' salaries to the level of other industries in the town even though sales volume has not increased.

There are several methods of reducing selling costs. Perhaps the stock should be rearranged so that the salesman will lose less time in getting the goods requested by the customers. Perhaps the self-serve plan should be adopted. Perhaps some lines are dead and should be replaced by lines in greater demand. Perhaps the store's total sales have declined while it has kept all its employees.

A retailer with several salesmen will usually find that the volume of sales and percentage sales cost will vary greatly among individual salesmen depending on the goods sold, the non-selling duties of the men, and the quality of their salesmanship. After he makes allowances for the first two factors, type of goods sold and non-selling duties, there still remains the problem of variations in sales ability among the different salesmen. The retailer is then face-to-face with the need for hiring better salesmen, for improving the training of his salesmen, or for better methods of reward that will induce them to exert more effort and to work more intelligently.

The owner of a large store said that his sales costs were considerably above the national average for his line of merchandise. To reduce the expense, he hired women to sell in some departments as they could be employed at somewhat lower salaries than men. Another practical method for large stores is to arrange the merchandise so that those lines which the consumers can select for themselves are placed in one section that can be operated on a self-service basis. Some stores may reduce expenses by paying salesmen on a straight commission basis.

The store that is not large enough to operate a self-service

section can economize on labor by using open displays and encouraging customers to wait on themselves and bring their goods to a wrapping table beside the cash register. Some merchandise can be placed in compartments on tables and plainly labeled as to price and size so that customers can make their own selections. A salesman should be available to help customers who have difficulty in locating or selecting merchandise. In this way a smaller number of employees may be used without reducing the sales volume of the store.

Laws applying to employment. In his relations with his employees the retailer is affected by many laws. These regulations, which vary from State to State, include the maximum hours of work for women (and sometimes for men), the minimum wages to be paid, and the age at which minors may be employed.

Retailers must pay both a State and a Federal unemployment compensation tax. State laws vary and affect retailers with a minimum of from one to eight employees, whereas the Federal tax applies to all employers with one or more employees. Many states have workmen's compensation laws that require the retailer to carry insurance against accidents to employees.

Retailers must pay the Federal old age retirement tax (social security), a part of which is deducted from the employee's wages, and must withhold the Federal income tax for those employees making more than the minimum amount. The social security and income taxes must be forwarded to the Federal Government at stated intervals. Details as to these deductions and payments may be obtained from the Treasury Department or from the district collector of internal revenue.

Questions

1. Of what aid are job analyses in selecting employees?
2. What are the sources of employees for retail stores?
3. What is the advantage of employing people who have had some college training but have not graduated?
4. What qualifications should prospective retail salesmen have?
5. What are the two parts of the interview?
6. What facts should be obtained about a prospective employee? What is the significance of the various facts obtained?

7. What are the most important questions to ask an applicant for employment?
8. What is the value of references?
9. In what should employees be trained?
10. What is business leadership? What qualifications should a business leader have?
11. What are the various methods of paying retail salespeople?
12. What are the advantages of the straight salary method? The straight commission? Salary plus a commission? Salary plus a bonus?
13. What are the disadvantages to the store of each of the above methods of payment?
14. How may selling costs be reduced?
15. What are some of the laws which apply to employment?
16. The personnel work of Arnold and Company, a department store, is under the supervision of the Superintendent of Operations, who acts as the company's Personnel Director in addition to his other duties.

    Mr. Moultrie, the Superintendent of Operations, has two assistants who work directly with him. Other people under his supervision are in charge of employment, training, job analysis, time keeping, welfare activities, and other personnel work.

    At the present time Arnold's is an establishment of approximately 5,300 employees. The total number of employees varies from about 4,800 to 6,000 individuals. Many hundreds of additional employees are required during the holiday season.

    Most of the new employees for the store are secured from the names on file in the store's own employment bureau. The majority of the office help however comes from the public employment offices of the city. For specialized positions within the store, advertisements are inserted in the local papers to attract the needed individuals.

    Periodically vocational counselors in the city high schools are contacted and informed of positions open and job opportunities for high school graduates. College recruiting also makes available recent graduates of nearby institutions.

    The actual hiring of new employees is taken care of at the store's employment bureau where applicants are selected either in the Nonselling Section or in the Selling Section of the bureau. The Nonselling Section obtains such employees as janitors, carpenters, window trimmers, elevator operators, and other service employees, and the Selling Section procures individuals for positions of salespeople and floormen.

    During the initial interview of all applicants, an application for employment is filled out for screening purposes. The indi-

viduals who seem best qualified for work with Arnold's are then invited back for a second interview at a later date. In the meantime, however, references on the application blank are checked and the form is approved by the interviewer.

During the second interview, a more complete application form is filled in and the applicant is taken to the department where he is to be employed and introduced to his supervisor. This, of course, is accomplished after an agreement is made as to wages and working hours. In all cases the head of the department has the final word of approval for a new employee.

Before the new employee actually begins work, he makes a trip to the Records Office where information regarding wages, home address, and other personal data are recorded, including also a pay number and locker assignment. After the new member has finished at the Records Office, he is taken to the Medical Department where he undergoes a physical examination and is certified fit for employment by the medical examiner.

With all the preliminaries completed, the employee is now ready for orientation in the training department.

Outline a training program for new inexperienced salespeople at Arnold's.

C. Buying and Pricing

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Buying: What, When, and How Much to Buy

IN PURCHASING merchandise for a retail store, what to buy, how much to buy, where to buy, when to buy, and how to buy must be considered. Because each of these phases of buying has subtle ramifications and interrelationships, only the more obvious ones will be discussed.

What to Buy

The fundamental principle of buying for a retail store is to buy only what can be resold profitably. This means that the store must have the right merchandise on hand, have it when it is wanted, and have it at the right price. Any mistake in applying this principle results in higher merchandise costs to both the store and the community.

Selecting the lines of merchandise. In determining what to buy, the new retailer must begin by deciding what lines of merchandise he will carry in his store. Some of the factors which he should consider in making his selection are as follows:

1. Lines of merchandise handled by existing stores in the community. When selecting the proper lines for his own store the retailer should ascertain what merchandise is already handled by other stores in the community. It may be that a certain line is in strong demand in a community but that other stores with established patronage already carry adequate stocks. If a new dealer elects to stock this line, he will be faced with sharp competition. However, it may be that these other stores carry

incomplete stocks. For example, both a department store and a hardware store may handle sporting goods but their stocks of tennis racquets, golf clubs, baseball equipment, and other sporting goods are small. When a customer wants superior quality or a particular style, he must wait for one of the stores to order it. Perhaps the men in charge of these departments have no particular interest in nor knowledge of sporting goods. Sporting goods, therefore, may be a logical line for a new store to carry, provided it maintains more complete stocks than the other stores and does a better job of displaying and selling the merchandise.

2. The retailer's knowledge and interest in the line. The retailer should consider his own knowledge and interests when selecting merchandise lines for his store. When it is evidently profitable to sell a line about which he knows little, he should study the merchandise until he develops an interest in, and knows much about it. For example, to sell kitchen utensils, household hardware, and cleaning supplies it may be desirable to employ a woman, and preferably a mature woman, who looks like a housewife.

3. Ability to dominate the retailing of a line of merchandise in the community. A store should not handle a line unless it can carry stocks sufficient to make a good showing in competition with other local stores. It is usually desirable, though not always possible nor practical, to dominate the line in the trading area. Instead of trying to carry a few articles in many different lines, it is usually preferable to select the lines best suited to the store and the community, and to carry enough of them to make attractive displays and to attract customers. The amount of capital and space, however, are limiting factors.

4. The merchandising policy of the store. Some retailers follow a policy of carrying complete stocks with the object of establishing a reputation for having stocks from which the customer can always fill his needs. Some of the lines in such a store, of course, will sell slowly. Other retailers follow a policy of maintaining complete stocks only for those articles that are in greatest demand. Some sales will be lost because of thin lines

of merchandise but the store economizes on space and capital. Each of these policies has its advantages.

Sources of information on what to buy. The lines of merchandise which a store carries usually will need to be revised and brought up to date to meet changing conditions. To realize this it is only necessary to compare the merchandise handled by department stores, drugstores, and hardware and grocery stores in past years with what they handle at present. It is essential that the retailer keep informed as to the nature of the changing demand for his different lines of merchandise. His customers are exposed to new products, new ideas, and new uses of merchandise and consequently their demands for merchandise change. Several sources of information are available for the retailer to consult in determining what to buy. Some of these are as follows:

1. Salesmen representing wholesalers or manufacturers. The capable salesman is well aware that it is to his best interest to sell the retailers on whom he calls only what they can resell profitably. Consequently, he thinks in these terms. Since his range of contacts extends from retailers located in the different trading areas in his territory to the representatives of wholesalers and manufacturers in wholesale markets, he usually possesses much worth-while information. It is to be expected, however, that he will be biased in favor of the merchandise which his firm is wholesaling or manufacturing.

2. Trade journals. Every major trade is represented by one or more journals devoted to news and problems of the trade. A retailer should subscribe to at least the leading trade journal in his field. Information obtained from one issue may be worth several times the cost of the subscription. New merchandise, new equipment, new systems, and new government regulations are discussed in these journals. From a study of the merchandise featured in the advertisements or discussed in articles the retailer can determine if it would meet the requirements of his customers.

3. Style and trade shows. Some of the major lines of merchandise are displayed or demonstrated at annual or semi-

annual trade shows. Examples are the furniture shows, gift and art goods shows, and men's and women's wear style shows. At these shows manufacturers display new designs and solicit orders. The retailer, from his contacts and observations at these shows, can form a better judgment of the merchandise which he carries and should carry.

4. Other stores in the trading area. The stocks of competing stores are another source of information as to what to buy. The fact that a competing retailer is carrying certain merchandise is not necessarily an indication that the new store should sell it. The first retailer may have made a mistake in his selection. Department stores, general stores, and variety stores carry merchandise which is also stocked by specialty stores. These competing stocks should also be examined from time to time. Considerable information concerning price, quality, and kinds of merchandise can be obtained from such an examination. In department stores the function of examining the stocks in competing stores is delegated to the comparison bureau.

5. Salesmen. Both from the point of view of sound management psychology and to obtain the needed information on what to buy, the salespeople should be asked for their opinions. If salespeople have a part in selecting the merchandise they are likely to be more enthusiastic about selling it. They feel as though they have an opinion or judgment to justify. If they are consciously or unconsciously prejudiced against the merchandise, the merchandise may sell slowly.

6. Store records. A store with adequate records has a valuable reference source for determining what to buy. The record systems used can be designed with one of their specific objects being to furnish such information. Proper sales records indicate what has sold and trends in sales. These trends show which articles are increasing in sales volume and which are decreasing. This information indicates how much of each article to buy. Stock records that show slow-moving merchandise (shelf-warmers) provide useful data on what not to buy.

The large store finds it practical to use a stock control system based on the physical unit of merchandise. From the informa-

tion gathered by this system, reports on slow-selling and fast-selling merchandise are prepared. The store may also use a want-slip system whereby salespeople advise the buyer of merchandise which is (a) approaching the low-stock level or (b) frequently requested by customers but not carried by the store. Records of merchandise returned to the store suggest what should not be bought.

Use of the information. Information from the above sources should be selected and examined carefully in determining what to buy. One factor to consider in evaluating this information is the price lines which the store handles. It is not practical to carry goods in all price lines. Only that merchandise should be bought which can be sold profitably at prices suited to the section or sections of the market to which the store caters.

A second factor which should be considered in selecting merchandise is the providing of a proper assortment. Merchandise must be bought with due consideration for such features as size, color, design or style, and finish.

The current appeal of a given style is another factor to be considered in selecting many kinds of merchandise. Consumer preference for a certain style may change suddenly. To avoid serious markdowns, the retailer must constantly sift all available information for an indication as to whether or not a given kind of merchandise is going out of fashion. On the other hand when the trend of fashion is anticipated correctly, the retailer benefits from such judgment by an increased sales volume.

The package in which merchandise is placed has an influence on its salability. It may not be logical for the consumer to buy merchandise because it is attractively packaged but the fact remains that he does so. Among the several characteristics which make a package attractive or unattractive to the consumer are size, shape, color, and material out of which it is made. Consumer preferences in packaging styles also are subject to change.

What merchandise should be bought is also affected by the vendor who offers it. The merchandise offered by a wholesaler, for example, who is known to be dependable is to be preferred

over goods handled by one who is known to be undependable. The problem of selecting vendors will be discussed later.

The quality of the merchandise in relation to its price is a fundamental factor (if not the most important one) in the selection of the merchandise. A cornerstone of many successful retail stores is the retailer's ability to offer a better quality of merchandise for the price than do other stores. Large stores sometimes make use of testing bureaus to determine the quality of the merchandise they plan to sell. Buyers for both small and large stores, however, depend largely on personal inspection of the goods and the reputation of the vendor. Much helpful data can be obtained by inspection of the merchandise if laboratory equipment and methods are used, but this procedure is often impractical.

The brand policy of the store is another factor which affects the selection of merchandise. If it is the policy of the store to handle nationally advertised brands, these lines will be selected. A certain amount of prestige is often created for the store handling widely advertised brands. Furthermore, they may sell faster than relatively unknown brands.

Special purchases. Occasionally a retailer has the chance to buy special lots of merchandise at low prices: These may be job lots or distress goods bought from retailers, wholesalers and manufacturers who are going out of business or selling overstocks or trying to raise cash quickly. Some retailers have been very successful in handling special lots profitably. They are more often operators of large rather than small stores, and their establishments are more often stores located in shopping centers rather than in small neighborhoods or villages.

Before deciding to buy goods offered at special prices a buyer should be reasonably sure that the goods can be sold in his community. If they can, perhaps he can use them as a leader, advertise them, attract people to his store, and help to establish his store's reputation for low prices. If they are to be placed in stock for sale in the normal course of business, he should determine how the special purchase will probably affect the rate of stock turnover.

Job lots often contain many odd or end sizes, and articles

which sell very slowly. It is easy for a retailer to be misled by a low job lot price and to make unwise purchases. It is also easy for him to worry about some of the end sizes and consequently pass up a profitable purchase. Perhaps he can give the odd articles and the end sizes to charitable organizations and still make a better than average profit on the easily salable goods. In making such a purchase the retailer should evaluate the lot carefully by dividing it into three groups. In one group can be placed those items which will prove readily salable in the regular stock. In the second should be placed those articles which can be used as leaders or sold in a special sale. The merchandise which will be given away or carried in stock a very long time should be placed in a third group. By totaling his anticipated prices for the goods in the first two groups, he can determine how much he should pay for the lot in order to make a profit.

When to Buy

Several factors affect the time to buy. It is desirable to buy liberally in advance of a rise in wholesale prices. However, it cannot be determined with certainty when prices are going to advance. Although the retailer can develop skill in anticipating, rarely can he buy merchandise when the price is lowest and sell it when the price is highest. It is impossible to obtain and to weigh accurately all the information which affects prices at any one time.

When a retailer buys merchandise in excess of current needs, he enters the realm of speculation and leaves that of merchandising. He is expecting to make a large profit due to a rise in prices rather than the small profit allowed for in regular markups, by reselling the merchandise. Some retailers have at times profited by making speculative purchases. It cannot, however, be advocated as a policy for all retailers to adopt. The risk is too great. Prices decline as well as rise. A price decline is just as unpredictable as a price rise. The extent of any given price decline may be greater than the price rise which preceded it.

When wholesale prices are declining, some vendors as an

inducement to buyers offer to guarantee their prices against declines. That is, they promise to rebate to the retailer the difference between present prices and prices ninety or one hundred and twenty days hence. Often the rebate is the amount of the price reduction on goods in the buyer's stock when the price is reduced. Under some conditions such an arrangement may be satisfactory, but if the merchandise will not be needed for resale within a normal time, there is no advantage in such buying. If the vendor lowers his price, the lower prices are likely to be available to all retailers at that time. Refraining from buying would undoubtedly encourage the vendor to reduce his prices still further, whereas the placing of an important order will encourage him to maintain his prices.

When to buy also depends on how fast a particular line of merchandise is selling. During sellers' markets (such as existed in the war and post-war period) when merchandise can be sold as rapidly as it is displayed, orders are placed in excess of needs as there is little hope that all will be delivered within the season. In times when the rate of turnover is less rapid and the period required for delivery is predictable, the time to buy can be determined rather definitely.

The time to buy is also influenced by the terms which are available. When the demand for goods is strong, the terms on which they can be bought are likely to be less favorable than when the demand is less strong. In periods of normal business activity the strength of demand and the abundance of supply vary from season to season as well as during a single season.

The dates when trade shows are held often determine when merchandise is bought. These shows are held when retailers are normally buying. Manufacturers' and wholesalers' salesmen are present at the exhibits and showrooms and orders can be placed easily.

The store's schedule for promotional events, or sales, determines when orders for the merchandise will be placed. Purchases will be made so many days or weeks in advance of the sale.

How Much to Buy

Several factors must be considered in determining how much to buy but probably none is more important than the expected or planned sales volume. Future operations should be planned whether a store is small or large. There is more likelihood of accomplishing objectives if plans are made to accomplish them. The most important part of a store's operating plan or budget is the estimated sales for a future period. All other plans are based on sales.

It may be objected that too many unknowns are involved to permit the planning of operations with sufficient accuracy to make planning or budgeting worth the effort expended. In answer, however, it can be pointed that many stores both small and large make plans and achieve quite accurate results with them. Store operations receive more careful consideration, too. The retailer obtains a clearer understanding of his business and is better able to co-ordinate its various phases.

Future sales, of course, depend on future business conditions and the latter can not be definitely foretold. It is highly desirable for the retailer to form some judgment of his own about these conditions. Even if his judgment is wrong, his error usually can be corrected in sufficient time to permit the adjustment of plans. A merchandise plan must be a flexible program that can be altered when conditions warrant it.

For example, a store might make 8⅓ per cent of its sales each month of the year, but the sales of only a few lines of merchandise are so stable. For many lines of merchandise the sales in July and January are below average while those in December are above average. If the sales of a store are analyzed by months, it will be discovered that over a period of several years about the same percentage of sales is made in corresponding months of different years. A method of estimating total sales by months is to build up the estimate by lines of merchandise. If an estimate of total sales for the entire store has been made first, this figure may be compared with the total of various lines and any adjustments which seem necessary can be made.

The amount of merchandise planned to be on hand at the

beginning and the end of a period affects the quantity of merchandise which the retailer should buy. To attain a given sales volume, sufficient quantities of the proper assortments of merchandise must be on hand. It also may be necessary to achieve the established sales volume with a relatively low investment in the merchandise. In other words, a certain speed of sale or rate of stock turnover is desired. This may mean that it will be necessary to reduce the inventory before the end of the period or perhaps to increase it. Whichever must be done, the amount of merchandise to be purchased is affected.

A merchandise plan takes markdowns into consideration. The entire budget has as its goal a certain gross margin and a given net profit. Each line of merchandise or department is supposed to make a contribution to the gross margin. If markdowns are not planned, the department or line of merchandise will be unable to achieve the gross margin that has been set for it to produce. Consequently, enough merchandise must be bought to which a markup percentage (which includes an allowance for markdowns) when applied will yield the planned gross margin.

In the same manner merchandise shortages must be anticipated. When the merchandise actually on hand is compared with the amount indicated by the stock records, it will be discovered that the quantity in stock is more or less than the written records show. If the physical inventory shows less than the book inventory the difference is due to errors in bookkeeping, loss in the physical handling of some merchandise, incorrect measurements of quantities sold, errors in counting the merchandise on hand, and to pilfering. Whatever the cause of the shortage, it should be taken into consideration when planning the quantities to be bought, otherwise a planned gross margin cannot be realized.

Discounts given to employees and others should be planned for in the same way as are markdowns and shortages. All represent reductions from the planned original retail price of the merchandise and must be taken into consideration if the anticipated results are to be attained.

At the time when the decision is being made on how much

merchandise to buy, there are usually some orders for merchandise which have not been received. These outstanding orders must be considered when computing the amount of merchandise to buy. For example, assume that the information given below represents a store's activity for the six months' period beginning February 1. The figures are given at the store's selling price, that is, at retail.

Planned stock, February 1	$20,000
Planned sales	60,000
Planned markdowns	3,000
Planned shortages	200
Planned discounts to employees	100
Planned stock, July 31	25,000
Merchandise ordered for delivery during the period	4,000

The amount of merchandise which the store is open-to-buy or to receive into stock is calculated as follows:

Planned stock, July 31	$25,000
Planned stock, February 1	20,000
Planned increase in stock	$ 5,000
Planned sales	60,000
Planned markdowns	3,000
Planned shortages	200
Planned discounts to employees	100
Total merchandise needed	$68,300
Goods on order	4,000
Amount open-to-buy	$64,300

If the initial markup is 40 per cent, the management plans to buy the merchandise at 60 per cent of the retail price. The amount of merchandise which the store is open-to-buy at cost is $38,580. If conditions change, the plans would be adjusted accordingly. A buying plan is not something absolute. It is subject to change. On the other hand, operations can proceed according to plan if the latter provides for the most likely variations and changes. One condition which is variable is the opportunity to make certain advantageous purchases. As has already been pointed out, the benefits of special purchases may be more apparent than real. In the course of a season, however, opportunities to make special purchases are very likely to

occur; they need not disrupt the plans, but often may be fitted quite smoothly into the over-all program.

In planning sales and the quantity of merchandise which must be bought, consideration must be given to the promotional events, if any, which are scheduled during the season. Merchandise must be bought in sufficient quantity to meet the anticipated demand.

The terms on which merchandise can be purchased may have an influence upon the quantity purchased at any given time. Terms sometimes vary with vendors and with the condition of the market. Frequently, quantity discounts are allowed when merchandise is bought in certain amounts. Whether or not merchandise should be bought in the quantities for which the vendor allows important quantity discounts depends on several factors. These are discussed in the next chapter.

The season also has a bearing on the quantity of merchandise bought. An important portion of the requirements for a season may be bought in advance. As the season progresses sufficient merchandise can be bought to keep the stock at the planned level. Near the end of the season only small orders, if any, will be placed.

Questions

1. What factors should be considered in selecting the lines of merchandise to buy?
2. What information sources may a retailer consult in determining what to buy? Which are the most important?
3. The information from the various sources should be selected in reference to what specific points?
4. What should be determined before buying a job lot or distress merchandise?
5. What conditions affect the time to buy?
6. What factors should be considered in determining how much to buy?
7. *Given:* Planned sales for the year $20,000
   Planned inventory Jan. 1 5,000
   Planned inventory Dec. 31 7,000

   Find: Planned purchases.

8. *Given:* Planned sales for the year $30,000
Planned inventory Jan. 1 8,000
Planned inventory Dec. 31 6,000
Find: Planned purchases.

9. *Given:* Planned sales for the year $40,000
Planned markdowns 1,000
Planned shortages 500
Planned inventory Jan. 1 10,000
Planned inventory Dec. 31 12,500
Find: Planned purchases.

10. *Given:* Planned sales for the year $50,000
Planned markdowns 1,000
Planned shortages 400
Planned inventory Jan. 1 8,000
Planned inventory Dec. 31 9,000
Outstanding orders Jan. 1 12,400
Planned initial markup 40%
Find: Open-to-buy at cost.

11. *Given:* Planned sales for Jan. $60,000
Planned markdowns 3,000
Planned shortages 500
Planned inventory Jan. 31 80,000
Inventory Jan. 1 90,000
Sales Jan. 1-15 20,000
Returns to vendors 2,000
Markdowns Jan. 1-15 1,000
Shortages Jan. 1-15 200
Merchandise received Jan. 1-15 30,000
Outstanding orders Jan. 15 17,500
Planned initial markup 44%
Find: Open-to-buy at cost Jan. 15.

12. How many items can you name that have been in steady demand for 50 years? For 25 years? For 10 years? Name products for which the demand has changed radically during the past five years.
13. Why does the demand for various articles change?
14. Why do fashions change? Who is responsible for the changes?
15. Are changes in fashion desirable? It is said, on the one hand, that changes in fashion cause loss to the consumers because the consumers discard goods before they are worn out, and loss to the dealers through mark-downs on out-of-fashion goods. On the other hand, it is said that fashion changes are good for the manufacturers and dealers because they stimulate sales, and for

the consumer because he tires of old products and derives pleasure (utility) from new things.

16. Why do some of the chain grocery stores carry more articles in stock than they did a decade ago?
17. Which can use small-order buying to better advantage, a dealer in a large city or one in a remote rural district?
18. How should a merchant determine when (under what conditions) to practice small-order buying?

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Buying: Where and How to Buy

Two major problems of buying remain to be discussed. These are where to buy and how to buy. Where to buy has three phases: geographical location, the selection of the type of vendor to patronize, and the choice of specific sellers.

Where to Buy

The location of vendors is of fundamental importance. It involves locating those who can furnish the right quality of merchandise in the right quantity and at the right price at the right time.

Location of sellers. Other things being equal, the nearest seller is the best source of goods. First, the near-by seller can give the quickest delivery. This means that the retailer can safely carry fewer goods in stock and so can turn his stock faster. If he runs out of an article, he can secure it more quickly from a nearby seller. Second, transportation costs are usually less. Third, the nearby seller is often a better source of credit. As pointed out in a previous chapter, the local wholesaler is closer to the retailer, calls on him frequently, follows his progress closely and so can often extend more liberal credit than will a distant seller. This advantage is especially important to the new dealer who has not established a credit rating and to the dealer who has a low credit rating. Fourth, salesmen from local houses often call more frequently than sellers from distant houses. They can assist the retailers in making up orders,

checking stock for shortages, and giving advice. Fifth, it is often desirable to handle locally made products because of the consumer goodwill which they develop. Such merchandise is usually well known in the community where it is made. Some members of the community are employees of the producer, while other residents see the plant, read about it in the local papers, know some of the employees, and perhaps own shares of its stock. Therefore a merchant likes to handle locally made products even if they are of no better quality and are less widely advertised than merchandise made elsewhere.

The choice of sources of goods is often between small local wholesalers (and manufacturers) and large wholesalers located at a distance. The distant seller may sell at lower prices, may carry wider assortments, or may sell products having strong consumer demand. If the prices of the distant vendor are lower than those of local wholesalers, the buyer must balance the saving in price against the advantages of quicker delivery and closer personal relations with local sellers. If both vendors ask the same price, the wide assortments, higher quality, or popular brands offered by the distant vendor must be balanced against the advantages of dealing with local sellers. Sometimes the local houses have lower expenses and can sell staples at lower prices than can the distant sellers. When this is the case, the proper course is to buy the staples from local vendors and the fancy or specialty goods from the distant, large sellers.

At times, some prestige or advertising value is created by purchasing goods from distant sources. The store that buys its women's wear in New York has more prestige than the store buying from a nearby wholesaler because New York is the leading U. S. fashion center for women's apparel. Hollywood has a high reputation as a source of sports clothes, and Grand Rapids for furniture.[1] There is a certain amount of prestige in being known as a "direct buyer." If a store buys direct, some cus-

[1] A Chicago mail-order house had to decide whether to ship dresses from New York to Chicago and fill orders from western customers there, or to forward the orders to New York and ship from there direct to customers. It would save time to deliver them from Chicago and delivery costs would be less because the dresses could be included in packages with other goods. On the other hand there was considerable value in advertising: "All dresses shipped direct from New York."

tomers think that it is an important concern and that it sells at lower prices because it eliminates the wholesaler's margin. Retailers may do some direct buying for the purposes of prestige, even though it is more economical to buy locally.

Buying from manufacturer and wholesaler. Some manufacturers sell only to wholesalers, others direct to retailers only, and others sell to both. Manufacturers in the last-mentioned group may sell (1) direct only to large retailers, or (2) sell to both large and small retailers but charge the retailers the same price as if goods were purchased from the wholesalers, or (3) sell to all retailers but not give the wholesaler full protection on prices. If a manufacturer sells only to wholesalers, the retailers must buy from the wholesaler or not handle the goods. Some manufacturers say that they sell only to wholesalers but class industrial buyers, institutions, and large retailers as "wholesalers." If a retailer is integrated and performs the wholesale functions, the manufacturer usually will sell direct to him. A successful retailer often tries to convince the manufacturer that he is integrated, that he buys in large quantities, stores the goods, discounts his bills, and so deserves a wholesale buying status. In order to claim a wholesale status, some retailers open branches until they have the requisite number of stores. Where price differentials are large, wholesale status may be a worth-while goal. However, if the price difference is relatively unimportant, the small retailer may be wise to buy from wholesalers in smaller quantities, turn his stock rapidly, and keep his capital liquid rather than tied up in large inventories. Most department and chain stores insist on buying direct from manufacturers and refuse to buy from wholesalers except for "fill-in" orders when goods are needed quickly.

Even though there is no price advantage in buying direct, some retailers do so in order to get new fashions quickly, to obtain fresh goods, or to secure complete assortments of a manufacturer's goods. When wholesalers do not keep up their stocks, goods may be obtained more quickly by buying from manufacturers.

Some retailers are so ambitious to be direct buyers that they do not consider all the factors involved. In transactions with

manufacturers transportation costs may be higher because of l.c.l. freight rates, and deliveries may be slower, credit less liberal, and collections stricter than in dealing with wholesalers. Cases have been reported of manufacturers insisting on their money in times of business depression and forcing the retailers into bankruptcy while wholesalers at the time were carrying the retailers until business improved and they could collect their accounts. The retailers were relatively small and unimportant customers of the manufacturers but they were so important to wholesalers that the latter tried to keep them in business.

It takes more time to buy from the manufacturers as more salesmen must be interviewed, or more visits made to the factory. Since wholesalers usually handle a variety of lines, the retailer can often secure all of his goods from one or a very few wholesalers. The wholesalers' salesmen call upon the retailers quite frequently and give them advice, particularly about local conditions and demands.

Type of wholesaler. The retailer may buy from one or more of several types of wholesalers: the full-line, full-service house; the limited service house; the cash-carry house; the drop shipper (in some trades); the voluntary group house; and the coöperatively-owned house. Often the retailer must choose between a local wholesaler with limited stocks who perhaps operates on a cash-carry or limited service basis, and a large full-line house located at a distance. The relative merits of these two types of vendors were discussed on pages 94-99.

In the food trade the problem of choosing between a private wholesaler on the one side and a voluntary wholesaler, or retailer-owned wholesaler, on the other is difficult. The efficiency of individual wholesalers varies greatly. An efficiently operated private service house may have lower expenses and prices than an inefficiently operated voluntary or coöperative house. Consequently the retailer's choice may be between individual houses rather than between types of houses.

A retailer may decide that he wants to join a coöperative and yet there may not be one convenient to his store. He must then join one at a distance or buy from another type of seller. The type of goods may be the deciding factor. He may buy some

from the coöperative and others from local privately-operated wholesalers.

Selection of individual sellers. There are several standards by which the retailer can make his choice of a seller. First, the suitability of the seller's merchandise to his clientele. Some retailers want high-priced or quality goods, others medium-priced goods, and others low-priced lines. Some retailers want the most advanced styles and others conservative styles. A second factor is the location of the seller. A third is the ethics of the seller. Some companies have high ethical standards and are known for their fair treatment of customers. On the other hand, some sellers are known for their sharp practices. A fourth is the financial strength of the seller. Other things being equal, a well established and financially strong house is preferred. However, a new house which has not had time to accumulate a large capital may give more service and be more attentive to the needs of its customers. The old established house may be complacent and self-satisfied. As companies get older their expenses often increase. Newly organized companies, by greater efficiency of operation, often undersell the established houses and gradually take their customers away. Thus, a retailer should not refuse to buy from a manufacturer or wholesaler simply because he is a newcomer.

The new retailer may have difficulty in appraising various sellers. The salesman for each house will probably claim the highest quality goods, the best service, and the lowest prices. How can the new retailer determine the truth of these claims? Perhaps the best way is to talk with other retailers. Since some retailers favor one company and some another, the new merchant should talk with established retailers in several towns. He may visit the sellers and look over their offices and warehouses. To get an accurate picture of relative prices may be difficult since one house probably features lower prices on some articles while a second house will be low on others. He may, however, compare their prices on a representative list of articles. Terms should be considered in comparing prices. What cash and quantity discounts are allowed? If the vendor is a coöperative house, what are the patronage dividends?

One way to rate sellers is by the success of their customers. If a seller has good merchandise and low prices, and if he serves his customers well, his customers should be successful. However, the success or failure of a store depends more on the retailer than on his suppliers. If a seller is to be judged in this way, a number of his customers should be interviewed.

The buyer may determine the financial standing and credit rating of sellers by consulting the bankers in the towns where they are located, or by looking them up in a credit rating book issued by a responsible agency. Full credit reports can usually be obtained at a relatively small cost if application is made through the proper channels.

Established merchants can rate sellers by their prices, the completeness of their stocks, promptness of delivery, information given, aid in selection of goods, and other services. Making such ratings is not easy and should be done carefully. As a rule no seller has the lowest prices on all articles. A dealer may decide that a certain house, Doe & Company, has good merchandise, low prices, good service; and consequently he buys from it. Salesmen for competing houses who want the retailer's business call on him and tell him about certain articles on which they have lower prices than Doe & Company. By constantly emphasizing their leaders they may cause the dealer to lose his faith in Doe & Company and change his source of goods or at least to divide his orders among several sellers. This problem is particularly acute for voluntary and coöperative wholesalers who have no salesmen. As one voluntary wholesaler expressed it, "My main difficulty is keeping competitors' salesmen out of the stores of my members." It is for this reason that voluntary houses require members to sign contracts to buy all or a very large portion of their goods from them.[2]

[2] One retailer had a franchise or agency from a voluntary wholesaler. He found that this wholesaler was low on some items but there were many articles he could buy cheaper elsewhere. The wholesaler warned him that he would have to purchase more goods from him or he would cancel the franchise. The retailer did not increase his purchases and the franchise was canceled. This retailer operated two stores; he employed salespeople to do the selling and assistants to help on different lines. He had the facts and felt no resentment against the voluntary for canceling the franchise.

A small retailer had a franchise with another voluntary wholesaler. Salesmen

It is said with much truth that the best way to rate a vendor is by the profit made on his line. Does his line have consumer acceptance? Does he carry popular styles? Year in and year out, is his proportion of good sellers high and his proportion of poor sellers low? If he has several poor-selling items in the line which must be marked down in order to sell them, the line may be unprofitable even though the original markup is high. A line with a lower markup may be more profitable if there are few markdowns, or if little has to be spent to promote its sale. Some dealers keep records of sales and expenses and determine profits earned by lines of the different sellers. Such accounting is expensive but is sometimes done by a large store selling fashion goods.

How many sources of supply? From how many sellers should a retailer buy? The small dealer may do well to give all his business to a very few sellers. Some argue that a retailer will do well to buy all of his goods from one wholesaler. He thus becomes a valued customer to this wholesaler who, in return, renders him good service in deliveries, advice, credit extension, and may help him in stock arrangement and display, and with his advertising and stockkeeping problems.

If retailers would concentrate their business, wholesale expenses would be reduced. Each wholesaler would have fewer customers and would need fewer salesmen. He would have fewer accounts on his books and his bookkeeping expenses would be reduced. Furthermore, the wholesaler's orders would be larger, which would reduce his percentage cost of assembling, shipping, and making out invoices. With decreased operating expenses, the wholesaler could reduce his prices and lessen the cost of distributing his goods. It is particularly important for small retailers to concentrate their orders. It has been found that when a small retailer divides his purchases among several wholesalers, all of them lose money on his business because his orders are too small to be handled profitably. If a small dealer will

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of competing wholesalers kept telling him of individual articles on which they had lower prices. He said, "I think it would pay me to drop out of the voluntary chain," but he was not sure. He had not made a careful comparison of prices. It is difficult for a small retailer to study the relative merits of different vendors.

give one wholesaler all his business, he then becomes a profitable customer, and the wholesaler may be expected to give him better service.

The retailer's buying operations are simplified by holding the number of vendors to a minimum. Less time is consumed in interviewing salesmen or filling out order forms. By concentrating his purchases, individual orders will probably be larger. This will reduce the time spent in keeping books, checking merchandise deliveries, and paying bills. Quantity discounts may be larger. Transportation costs may be reduced: fewer freight shipments of less than 100 pounds, less drayage, and perhaps carload shipments.

There are three objections to a retailer buying all of his goods from one seller. First, when the seller finds that he is getting all of a retailer's business, he may deliver goods of poor quality or render poor service. Many retailers feel that they must divide their business and play sellers against each other to prevent these practices. There is more danger of receiving poor quality goods in some lines than in others. For example, there is more danger when buying meats, fruits, vegetables than when buying standard packaged goods.

Second, no seller has the best quality or the most popular brands of all products. This is particularly true of wholesalers who have their own private brands. One wholesaler is known for his large assortment or high quality in a few lines while his competitors have better assortments or better qualities in other lines. It is thus argued that a dealer must buy from several houses to obtain the proper assortments of goods and brands wanted by his customers. Local wholesalers and cash-carry wholesalers may have the lowest prices on staples. They, however, have only limited lines. The retailer may patronize them for staples and buy his quality or fancy goods from other sellers.

Third, in case one seller is out of stock, it is desirable to have connections established with a second source.

Conclusion on number of sources. The retailer's sources of supply vary with the type of merchandise he carries and the size and location of his store. For the small or medium-sized retailer the usual advice is to limit the number of sellers patron-

ized but not to make all purchases from one house. It may be necessary to buy from more than one house to secure popular brands or to be able to secure complete assortments of the lines handled. On the other hand, it is usually advisable for the retailer to limit his number of sources in staple goods such as groceries and hardware to perhaps two, three, or four houses.

Having selected his sources of supply, the buyer should coöperate with them. However, he must not assume that the best sources today will always be the best sources. The character of the service rendered by a seller may change. Its management may improve or deteriorate. The owners or executives grow older, quit, retire, sell their interest, or die. When the founders of a business retire, its management is usually taken over by their sons or by hired managers who may change the policy of the house. They may not be as competent as the founders; service may deteriorate; the quality of goods may suffer; prices may be increased. It is obviously to the buyer's interest to give his business to another house if these things occur. Even if the service of a vendor does not change, a buyer may want new sources. The character of his trade may change so that he needs goods of a different quality. He may accumulate capital so that he can buy in larger quantities and pay cash. It may then be to his interest to buy from sellers catering to large accounts. He may be able to buy from producers or importers. He may be able to set up specifications for his goods, have them made to order, and sell them under his own brand. A merchant with a small store may find a near-by service wholesaler his best source. When his business expands, he may buy many goods direct.[8]

Relations with salesmen. Salesmen can consume a great deal of a retailer's time, but it is from them that valuable information is obtained. The salesmen often have bargains which they offer to buyers with whom they are on friendly terms. Naturally the salesman does not have important information or goods at ad-

[8] Two men started small stores in a boom year. Before they were well established, the country plunged into a depression. Both would have failed except that a wholesale salesman believed in them and had his house extend them credit enough to pull them through. Later, both men became very successful operators of chains of stores. They then bought most of their goods direct from manufacturers, but continued to give this salesman sizable orders.

vantageous prices to offer on every call, but the retailer does not know when he will have them. Some retailers seem to believe that it is their particular privilege to treat salesmen shabbily. The latter's time is wasted in waiting for promised interviews that are never granted. This is expensive for the vendor and accomplishes nothing for the buyer.

Terms of Purchase

The terms of purchase are often more favorable to the buyer when merchandise is plentiful. When a seller's market exists, vendors are less liberal with their terms because it is easy to sell merchandise. Although there is a tendency to standardization of terms in a given trade, the terms to different buyers may vary and some may be secret.

Net terms. When an invoice bears net terms, the amount appearing on the face of the invoice is to be paid within the stated period. The period may be 30 days from the date of the invoice. No discount is allowed for payment after the expiration of the period. There is no incentive to pay before the end of the period and payment may be deferred until the account is due.

Cash discount. To encourage prompt payment of invoices, many vendors allow a percentage deduction from the face amount of the invoices if they are paid within a specified time. If an invoice is not paid within the specified period, the net amount must be paid. The terms may be 2/10, n/30, which means that 2 per cent may be deducted from the amount of the invoice if it is paid within ten days after the date of the invoice. The full amount of the invoice is due 30 days after the date of the invoice. In other words, if an invoice bearing these terms is dated September 1 and the amount of the invoice is $100, payment of $98 (check or cash) is due not later than September 11. The full amount of the invoice, $100, is due not later than October 1.

The retailer should usually take all cash discounts. If he does not take them, it is generally assumed that he does not know his business or is short of capital and so is a poor credit risk. The

reason for this assumption is based on the significance of the usual cash discount. If a retailer fails to pay an invoice bearing terms of 2/10, n/30, it is equivalent technically to paying interest at the rate of 37.2 per cent per annum—usually expressed as 36 per cent. When the purchaser fails to pay the invoice by the end of the discount period of ten days, he pays $2 for the use of $98 for the next twenty days, at the end of which he must pay the full amount of the invoice, or $100. Since there are 365 days in a year, there are 18¼ twenty-day periods in a year. If $2 is paid for the use of $98 for each of these periods, a total of $36.50 would be paid. This would be at the rate of 37.2 per cent per year.

Quantity discounts. To induce retailers to purchase larger amounts, some vendors offer a reduction from the price at which a single unit or other established amount is sold. The larger the amount purchased, the larger the discount may be. For instance, a quantity discount of 3 per cent may be offered to retailers who buy in lots of 100 units, 5 per cent may be offered when purchases are made in quantities of 250, and 10 per cent may be offered when quantities of 500 are purchased. If a cash discount is allowed, it is deducted after the quantity discount.

Quantity discounts may be allowed on the total quantity purchased during a year. Whether or not a retailer should buy in larger quantities in order to avail himself of an attractive quantity discount depends on how fast he can sell the merchandise and how much it costs him to handle it. Attractive though the price may be when merchandise is purchased in large quantities, it may not be profitable to buy it if it can not be sold within a reasonable time.

Trade discounts. Some vendors use trade discounts in varying their prices. The discount varies according to the kind of buyer: a department store, chain store, independent retailer, or a wholesale merchant. The two reasons for a trade discount are the quantity purchased and the services performed by the purchaser. The larger retailers and the wholesale merchants are assumed to perform services which the smaller retailer does not perform.

Trade discounts are quoted as a percentage to be deducted from a list price. The list price is a base price which may be the resale price suggested by the vendor, or it may be a more or less arbitrary figure. The trade discount may be a single flat percentage as 30 per cent, or it may be a series of percentages as 25%, 15%, and 10%. In the latter case if the list price of an item was $120, the cost price to the purchaser would be $68.85. This is calculated by deducting 25% from $120. Fifteen per cent is deducted from the remainder of $90. From the remainder $76.50, ten per cent is deducted. If a cash discount of 2 per cent were also allowed, the net price would then be $67.47.

Dating. Terms which involve a cash discount include a discount period and a net period. Terms of 1/10, n/20 or 2/10, n/30 are regular or ordinary datings. The terms may be 2/10, n/30 R.O.G. in which case the discount period is ten days after the receipt of the goods. If the terms are 1/10, n/20 E.O.M., the discount period is ten days after the end of the month. Advance dating means that the vendor grants terms such as 2/10, n/30, September 1 although the goods may be delivered July 15. Advance datings are granted to encourage buyers to place orders during a period when the vendors are operating considerably below capacity. This is usually out-of-season. Terms are arranged so that payment is made during the normal buying period or season and the method is called seasonal dating. Extra dating terms are expressed as 2/10-50 extra. In such a case, the buyer has 60 days in which to take the discount. It is the custom in some trades for purchasers to take, and vendors to allow, a deduction called "anticipation" when the invoice is paid within the discount period. When anticipation is allowed, it is sometimes computed at the rate of 6 per cent per annum. If an invoice for $750 bearing terms of 2/10-60 extra is paid 70 days after the date of the invoice, 2 per cent would be deducted from $750. However, if paid 10 days after the invoice, the cash discount is taken, and from the balance of $735 interest at the rate of 6 per cent for 60 days is also deducted—an amount of $7.35. The amount due the vendor would then be $727.65. When money is plentiful and interest rates low, sellers often specify "no anticipation."

Advertising allowances. Some manufacturers make an allowance to retailers who advertise and display the manufacturer's products. The method of making the allowance may be by a reduction in the price of the merchandise, or by giving the buyer an additional quantity of merchandise which amounts to the same thing as a price reduction. This may seem attractive, but it may be more profitable to display and advertise merchandise which is in greater demand. To comply with the Robinson-Patman Amendment, advertising allowances must be available to all buyers on a proportional basis.

Transportation charges. Shipping costs are sometimes a subject of negotiation but merchandise is often shipped *f.o.b.* (free on board) *shipping point.* That is, the buyer pays the cost of transportation from the shipper's city. The terms may be *f.o.b. factory,* in which case a cartage charge may be made for delivering the merchandise from the factory to the freight station. If shipment is made by a truck line or if a railroad spur extends to the factory, no separate cartage charge is made. Should the terms be *f.o.b. store,* the seller pays all transportation charges. Sometimes the terms are *f.o.b. shipping point, charges reversed.* In this case the seller assumes all risks of transportation and pays the cost of transportation but later the buyer reimburses him for the amount of transportation.

Buying on consignment. To induce a retailer to handle their merchandise some vendors will offer goods on a consignment basis. In such instances the retailer is an agent and does not have title to the goods. Certain conditions make it advisable to accept merchandise on consignment while other conditions make it undesirable to do so.

A beginning, inexperienced retailer who is short of capital may find it desirable to obtain some merchandise on consignment in order to make his stocks more complete. He assumes fewer risks than if he purchased the merchandise outright. The risk of ownership remains with the vendor. If prices decline or the merchandise does not sell, it is the owner who loses. Even experienced retailers find it advisable sometimes to obtain merchandise on consignment. They desire to have the large sales volume which results from new goods that sell readily. When

a large promotional event is planned, it may be advisable to obtain merchandise on consignment, since the outcome is usually unpredictable. If considerable merchandise is purchased for an event and for some reason the expected sales volume is not realized, an important loss may be incurred or the rate of stock turnover may be reduced. As a hedge, some merchandise is obtained on consignment. If it does not sell, it can be returned to the owner. If it does sell, the store's patrons are adequately served and the store earns a profit.

On the other hand, when merchandise is obtained on consignment the control of its resale price may be left in the hands of the owner. This may limit the margin on the merchandise. As a matter of fact the retailer is acting on a commission basis. Since he does not assume the risk of ownership, he is expected to handle the merchandise on a smaller margin than would be the case for similar merchandise purchased outright. Merchandise which can be obtained on consignment may not be of superior quality or may be overpriced—thus the necessity for offering it on a consignment basis. A dispute between the retailer and the vendor may develop if the merchandise fails to sell.

How to Buy

Efficient buying is well organized and planned. In the small store the owner or designated salespeople do the buying.[4] In a large store the problem is greater and the nature of the buying organization more complex, as has been previously discussed.

The amount to be invested in each line of merchandise must be converted into the number of units to be purchased. The units must be distributed according to price lines and merchandise with the proper characteristics must be selected. This plan, of course, is based on definite merchandising objectives. Without a plan the buyer has but a vague notion of his objectives and his buying will reflect his inadequate forethought. Although the buyer's intuition may be good, it may not be good enough. It is better to formulate and depend upon a

[4] The buying organizations and the greater buying problems of larger stores have been discussed on pages 231-235.

plan rather than upon what seems to be a likely purchase. The plan should, of course, be adjusted to changing conditions when they occur. In any case, however, the buyer with a plan knows what he is doing. The large store does not and can not afford to operate without buying plans and the small store can not afford to ignore them.

The buying of staples which sell at a steady rate and which the store is normally expected to carry does not present a difficult problem. Once the desired quantity and assortment have been determined, the principal problem is to reorder when sales have reduced the amount on hand to a predetermined quantity. In determining this low stock level due regard must be given to the possibility of a delay in delivery or an increase in the rate of sales. The buying of fashion and seasonal merchandise presents a more difficult problem. Closer surveillance of the quantities on hand and the rate of sale are required. Reordering is not automatic.

Ordering may be done by telephone, by mail (from catalogs or price lists), by placing orders with salesmen who call on the buyer, or by placing them while on a trip to wholesale markets. Visits to wholesale markets are time-consuming and expensive for the small retailer. Because of the social activities which may be combined with a buying trip, more trips are probably made than are necessary.

Experienced buyers advise that on trips to the market vendors of low-priced, medium-priced, and high-priced merchandise should be visited even though the retailer handles merchandise in only one of these price classes. The object is to improve the buyer's judgment as to the relationship between prices and quality. They also recommend that orders not be placed until the market has been covered, unless there is no question of doubt concerning the advisability of purchase. The persuasiveness of a salesman may remove, temporarily, any doubt which a buyer may have concerning a particular selection.

Questions

1. What are the advantages of a near-by source of supply? What may be the advantages of a more distant seller?

2. What are the advantages in buying direct from manufacturers? The disadvantages?
3. What are some standards by which individual sellers may be selected?
4. From how many vendors should a retailer buy?
5. What are the possible disadvantages of buying all goods from one seller?
6. What is meant by net terms?
7. Terms of 1/20, n/30 are equivalent to what annual rate of interest?
8. The United Appliance Company offers a washing machine to retailers on terms of 2/10, n/30 at $40 each; the Atlas Appliance offers the same machine at $43 on terms of 6/10, n/30. Assuming that a retailer would take advantage of the cash discount, from which of these companies should he buy?
9. An invoice is dated May 2 and bears terms of 2/10, n/30. The amount of the bill is $150. The merchandise was to be shipped f.o.b. destination. The retailer paid freight of $5.88 when the merchandise arrived on May 4. He sent a check for $78.40 on May 6 and on May 12 wants to mail a check for the balance due on the invoice. What should be the amount of this check?
10. The Emporium Department Store receives an invoice from the Eclipse Manufacturing Company dated April 12 and amounting to $250. The terms are 2/10, n/30, f.o.b. destination, charges reversed. On April 22 a check is mailed to the Eclipse Co. What should be the amount of the check?
11. Millers' Dry Goods Store receives an invoice amounting to $800, dated March 4, and bearing terms 2/10, n/30 on a purchase of furniture. What should be the amount of the payment on March 14?
12. The Grand Rapids Furniture Company offers Roland's a choice of terms: 5/10—90 extra, or 6/10, n/30 on a purchase of furniture amounting to $600. Which terms should Roland's accept? Explain.
13. Reid's received an invoice dated September 24 amounting to $300 and bearing terms of 2/10, n/30 and trade discounts of 20%, 10%, and 5%. The invoice is paid October 4. What should be the amount of the payment?
14. What are the advantages of buying on consignment? The disadvantages?
15. How should a retailer plan his buying?

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The Problem of Pricing

GOOD merchandising requires having the right goods, at the right time, at the right place, and at the right price. In order to have merchandise at the right price, certain price policies should be adopted. The technique of using price policies must be understood if the policies are to be applied correctly.

General Price Policy of the Store

The retailer must determine his general policy as to price. He may adopt any of four general policies: (1) prices somewhat higher than those of competitors; (2) prices in line with the prices of competitors; (3) prices below those of competitors; or (4) a liberal use of leaders.

Selling at the market plus. The store which sells at prices somewhat higher than those of competitors bases its appeal on quality, variety of merchandise, and service. Such stores carry a wide selection of goods and will have some that sell very slowly. These stores make their appeal by having goods not available elsewhere or by having goods of high quality. The consumers may say: "You can get it at Blanks," or "You can be sure of the merchandise you get at Blanks." When such a reputation is well established in a community, the store will usually have a sufficient sales volume to make business profitable. These stores usually offer more services than do their competitors. Just which services to offer, and whether to attempt to charge higher prices because of the fact that these services are

offered is a decision that should be made only after a survey of the market and the activities of competitors.

Some of these stores are located in central shopping districts or suburban areas where rent, labor, and other expenses are high in relation to sales. They may be located in areas where competition is not especially strong or aggressive. In the first instance they may charge higher prices because their own expenses make it necessary; in the other, because they wish to take advantage of their favorable situation.

There is a sales appeal in a higher price. There is often a high degree of correlation between price and quality. To the extent that this is true in the community, a certain amount of trade will be attracted by high prices. There are those who get satisfaction from explaining that their purchases came from a store known to have high quality, high prices, and superior service. The inference is that the purchaser is a person of discriminating taste and affluence.

Selling at the market. The majority of stores sell at prices in line with other stores in their area. This is called "selling at the market." Retailers following this policy believe that they cannot obtain higher prices than their competitors and there would be no point in selling for less. The adoption of this policy will raise the question—who are the retailer's competitors? Are they the cash-carry stores, the cut-price stores, the chain stores, the service stores, or the stores in the next town? Is the downtown store a competitor of the store in the outlying shopping district? There is no one completely satisfactory answer to such questions. It may be that the service store need not meet the prices of the nearby cash-carry store; often consumers do not compare prices in these two types of stores. About the best general statement that can be made is that a store's competitors are the stores most frequently patronized by the store's customers with, perhaps, some allowance for service rendered.

Next comes the question—what are the prices in competing stores? Large stores employ comparison shoppers who visit competing stores and report on their prices and stock. The small retailer may note prices of goods displayed in his competitors' windows, and in his competitors' advertising. Whole-

sale salesmen may provide some information. He can visit his competitors' stores, the frequency depending upon the personal relations between them. Customers furnish a certain amount of price information, but it is sometimes misleading, since they may mention only the prices of specific items which the competitors are using as leaders, or are closing out, or which are damaged.

Selling at the market minus. The store which sells at prices lower than its competitors is selling at the market minus. The lower prices may be expected to increase sales, increase the rate of stock turnover, and reduce expenses, so that the profit will be increased. It is believed that low prices make the strongest appeal, being most attractive to the majority of the customers. Some of the most successful retailers have been those who have kept their expenses low, their prices below those of their competitors, and still have made larger than average profits. To do this means that the retailer's operating expenses must be much lower than his competitors'; that he must have an economical source of goods; or that he both has low expenses and can obtain low-cost goods. The small store usually must have lower-than-average expenses to make a high rate of profit, although some advantage may be obtained in buying from coöperative and voluntary wholesalers. The large store may buy many of its goods direct and more frequently obtain job lots at favorable prices. If a retailer can hold his expenses down, he may be able to undersell his competitors, and thus increase his sales until he he is large enough to secure a wholesale buying status. As a general rule, the retailer in the small town has lower expenses than stores in larger communities. Such retailer may be able to undersell the stores in nearby cities.

Selling at prices lower than his competitors' is sometimes a dangerous policy for the retailer. Competitors often respond by cutting their prices. The store selling at the market minus must, if it sticks to its policy of underselling competitors, reduce its prices again. Such retaliation often leads to a price war which may end in the failure of one or more stores. If the store selling at the market minus has lower operating expenses and a reasonable amount of capital, it stands a good chance of

survival. Such a store desires to keep its prices down and yet avoid an out-and-out price war. Healthy price competition is one thing. A bitter price war is another. Perhaps the wisest procedure for the store operator is to refuse to enter a price war, maintain his prices, and use leaders to combat the competitor. The skillful use of leaders may be an effective weapon temporarily. The competitor may soon tire of the fight and raise his prices to their former level. If he does not, the retailer must reconsider his policy. Perhaps the competitor also has low operating expenses and has elected to reduce his prices. If so, the retailer probably should change his policy and not reduce prices to the level of his competitor. If, however, he chooses to retain his policy of selling at the market minus, he must reduce prices throughout his store.

Use of leaders by the promotional store. By a promotional store is meant one that makes liberal use of leaders, one that applies price strategy, and one that makes a liberal use of advertising and window display to feature its leaders. A promotional store is sometimes called a "cut-price" store. Competitors often accuse the merchandising store of charging exorbitant prices on "blind" articles. By blind articles are meant those items with prices not generally known to the public or articles the qualities of which can not be readily compared.

The promotional store may have low prices on widely advertised, well-known merchandise and on merchandise of known value, and retain the usual or higher prices on articles whose value is unknown to the public. The promotional store asks: "What is an attractive price for this article? How much will the public pay for it?" rather than "How much did it cost?" or "What will I have to get for it to make a fair profit?"

Leaders and loss leaders. A leader is an article sold at a very attractive price, usually below the general market level, on which the margin is less than normal.

There are two meanings of the term "loss leader." According to one meaning, it is an article priced below what it cost the retailer. According to the second meaning, it is an article which is priced below its cost plus the expenses involved in selling it. To illustrate, the invoice cost of an article is $2.70, and

the expenses involved in its sale are 90 cents. If it is sold for $3.30 it is a loss leader according to the second meaning but not according to the first. If it is sold for $2.30 it is a loss leader according to both meanings. If this article is sold for $3.68 it may be a leader but not a loss leader.

Loss leaders are used to attract customers to the store in the expectation of selling them other goods at a profit. There is little to be gained by using loss leaders unless they are well advertised. If the store is on a street with very heavy traffic the window advertising may be sufficient. In the majority of cases, however, other forms of promotion will be needed.

Leaders are used to increase store traffic. A good traffic builder should be an article with a wide appeal and a known value. Hardware stores have seldom used leaders because so many of their sales are made to people who have definite needs and because most of their merchandise is durable. Quickly consumed goods that have to be rebought constantly are often used as leaders by grocery and drug stores.

Determining Selling Prices

There are many factors to be considered in determining the proper selling prices. Among these are the retailer's expenses, the prices of competitors, whether or not an item is to be used as a leader to build traffic in the store, and the value of the article to the consumers. The markup process will be discussed first.

Markup. In computing the cost of his goods, the retailer should deduct all quantity discounts from the invoice cost, add to the invoice amount all transportation costs involved in getting the goods into his store. There is a difference of opinion as to the procedure in deducting cash discounts. In some trades they are taken so regularly by buyers that it is exceedingly difficult for a retailer to overlook them and stay in business. When this is the case, they must be deducted from the list price to get the net cost to the buyer. If, as in some trades, the buyers do not take all their cash discounts, the deduction should not be made in arriving at the cost of goods since the retailer does not

know whether or not he will take the discount. Such retailers consider cash discounts as *other* income in their profit and loss statements.

If a retailer has expenses equal to 25 per cent of his sales and he desires to make a profit of 5 per cent, he must mark up the article 30 per cent on selling price. Thirty per cent of cost will not give 30 per cent on the retail price. If the article cost \$7.00 and 30 per cent is added to the cost, the price of the article will be \$9.10 (\$7.00 × .30 = \$2.10; \$7.00 + \$2.10 = \$9.10). But the price of \$9.10 allows the dealer as margin only 23.1 per cent on the retail price: \$9.10 — \$7.00 = \$2.10 markup. $\frac{\$2.10}{\$9.10} = 23.1.$ Since the dealer has operating expenses of 25 per cent, he would actually lose about 2 per cent on this sale. The story of the retailer who bought a suit of clothes for \$24 will illustrate this point. This retailer marked his suit to sell at \$30 thinking he was making a 25 per cent markup. When a friend came in he told him that he would let him have the suit at cost; so he deducted 25 per cent from \$30 and sold his friend the suit for \$22.50. He still wonders what happened to the \$1.50.

When the percentage of markup is based on selling price, the selling price is equivalent to 100 per cent. If the retailer needs 30 per cent of the selling price to cover his expenses and desired profit, the cost must equal 70 per cent (100 per cent minus the 30 percent markup). The cost of the article was \$7.00 or 70 per cent of the selling price. Therefore, to obtain the selling price divide \$7.00 by .7. This gives \$10, the selling price of the article for a 30 percent markup on the selling price. If the article is sold for \$10.00, a 30 percent margin is obtained.

Traditionally, the small retailer has applied a percentage to the cost of the merchandise when he has used the markup method. He did this because his first thought was of the cost of the merchandise. His next thought was of the proportion of the article's cost which would be necessary to cover his expenses, allow him a profit, and which, when added to the cost of the article, would not yield a price higher than most consumers would pay. Marking up merchandise on the basis of cost was an easy method of arriving at a price. He did not, and most of

them still do not, operate with modern merchandising plans. Modern retail management, however, calls for planning based upon sales being equivalent to 100 per cent and thus derives a markup which covers expenses and allows a profit.

It is true, of course, that taking cost as being equivalent to 100 percent, the same selling price can be arrived at as when selling price is taken to be equivalent to 100 percent. In other words, either cost price or selling price may be considered equivalent to 100 percent and the same selling price may be obtained. Only elementary arithmetic is involved. The formulas which will give the same selling price are as follows:

1. When selling price is taken as being equivalent to 100 percent

$$\text{Selling Price} = \frac{\text{Cost}}{100\% - \text{Markup }\%}$$

2. When cost is taken as being equivalent to 100 percent

$$SP = C\left(1 + \frac{MU}{1 - MU}\right)$$

To illustrate formula 1, using the figures on page 340

$$SP = \frac{\$7.00}{1 - 30\%}$$

$$SP = \frac{\$7.00}{100\% - 30\%}$$

$$SP = \frac{\$7.00}{70\%}$$

$$1\% = 10 \text{ cents}$$

$$SP = 100\%$$

$$SP = \$10.00$$

To illustrate formula 2, using the same information,

$$SP = \$7.00\left(1 + \frac{30\%}{1 - 30\%}\right)$$

$$SP = \$7.00\left(100\% + \frac{30\%}{100\% - 30\%}\right)$$

$$SP = \$7.00\left(100\% + \frac{30\%}{70\%}\right)$$

$$SP = \$7.00 \times 1\ 3/7$$

$$SP = \$10.00$$

Markup table. The retailer need not make such detailed computations on every article. He may use a table showing selling prices for articles with various costs to yield the desired percentages of markup. Let us say that when goods are priced by using fixed percentages of markup, that the percentages are 20, 25, 33⅓, and 40 per cent. For an article costing $1, the selling prices are as follows:

Markup percentages.......	20%	25%	33⅓%	40%
Selling price..............	$1.25	$1.33	$1.50	$1.67

The merchant then constructs his table by multiplying the above figures by the various cost prices. A section of his table is:

COST PRICE	MARK-UP 20%	SELLING PRICES 25%	33⅓%	40%
$0.10	$ .12½	$ .13	$ .15	$ .17
.12	.15	.16	.18	.20
.19	.24	.25	.28½	.32
.90	1.08	1.20½	1.35	1.50
1.50	1.87½	2.00	2.25	2.50

Mark-downs and shortages considered. If a retailer considers only his expenses and the profit he desires in determining a markup percentage for a line of merchandise, he may still fail to make a profit. Almost every store finds it necessary to markdown some merchandise before it can be sold. For one reason or another shortages of merchandise occur and discounts are given to employees and others. None of these items are likely to be included among expenses. All may need to be estimated if adequate records of them are not kept. The consequence is that an initial or original markup percentage must be determined and applied if expenses are to be covered and a profit is to be earned. Expenses plus profit are equivalent to gross margin or the maintained markup.

The formula for determining the initial markup which should be applied to a line of merchandise is:

$$\text{IM} = \frac{\text{expenses} + \text{profit} - \text{cash discounts} + \text{discounts to employees and others} + \text{markdowns} + \text{shortages}}{\text{sales} + \text{markdowns} + \text{shortages} + \text{discounts to employees}}$$

Sales are equivalent to 100 per cent. The derivation of initial markup can be illustrated as follows:

Expenses	28%
Net profit	4%
Cash discount	2%
Discounts to employees	1%
Markdowns	7%
Shortages	1%

$$\text{Initial markup} = \frac{28\% + 4\% - 2\% + 1\% + 7\% + 1\%}{100\% + 7\% + 1\% + 1\%}$$

$$\text{Initial markup} = 35.78\%$$

The practical figure to use would be 36 per cent. It may be necessary to adjust any derived initial markup percentage due to other pricing factors which must be taken into consideration.

When the selling price equals 100 per cent, cost plus markup equals 100 per cent. The cost percentage is referred to as the cost complement. If the markup percentage is 37½ per cent, the cost complement is 62½ per cent. With one given, the other is easily found.

Pricing individual articles. Although operating expenses are a basic factor in determining selling prices, it is necessary to consider other factors such as the prices charged by competitors, the value of the article to the consumer, the use of the article as a leader, and the desirability of even or odd prices.

How various factors enter into consideration may be illustrated by an article with a net delivered cost of $39.84 per dozen. A markup of 33⅓ per cent on the selling price will give a price of $4.98 each. A competitor may be selling the article at $4.50. To price the article at $4.50 would allow only a 26.3 per cent markup. This would result in a loss if the retailer's expenses on this article are higher than 26.3 per cent. The loss may be small, however, and it may be desirable to price the article at $4.50 and stay in line with the competitor.

Other possibilities are to price the article at $4.39, to discontinue the article, to replace it with an article of superior

quality selling at a higher price, to replace it with an inferior article which can be sold profitably at $4.50, or to try to buy the article at a lower price so that it can be sold profitably at $4.50.

The competitor's price may be ignored and as many sales as possible made at $4.98. If it is a "blind" article this may be desirable. On the other hand if the article will make a good leader, the $4.39 price may be better because it is below the competitor's price. If it is the policy of the store to handle high quality merchandise it may be well to replace the article with one of better quality at a higher price. A higher quality product may be added and the old product sold at $4.50; but the quality of the better product will be pointed out to the customers in an attempt to "trade them up." The latter is sometimes a good policy but it takes too much of the salesman's time to do it often with low-priced articles. Generally speaking, it is poor policy for a store with a quality reputation to sell inferior goods in order to match a competitor's price. A retailer's reputation should not be sacrificed lightly. The retailer may be able to find another source that provides the item at a price low enough so that he can sell profitably at $4.50.

Even and odd prices. Many articles are sold for 5, 10, 25, 50 cents and $1.00. These prices require a single coin. Many dealers formerly priced their goods in such even prices, but this method has been abandoned by several retailer groups. The department stores and mail-order houses have long used odd prices extensively to give the impression that their prices were lower. Thus they priced the article at $2.98 instead of $3.00. In the grocery field, the chain stores early adopted the policy of odd prices. It seems that many retailers formerly priced their goods at an even price above the price fixed by their normal markup. If their normal markup resulted in a price of $4.89, they made the price $5.00. Retailers, by using the odd prices derived from the application of the markup percentage, caused others to follow their example and the use of odd prices became more general.

In addition to the use of odd prices by the retailers, the levy-

ing of various sales and excise taxes by states and the Federal Government has further contributed to the widespread use of odd prices. The existence of a sales tax does not of itself cause the retailer to use odd prices. He may still use even prices, but the addition of the tax usually results in an odd total price to the consumer. If the state law does not prohibit the practice, the retailer may include the tax in marking his goods and advertise that he does not add the tax. Since these taxes are a nuisance to most people, this procedure may be desirable. The retailer should, however, examine the law in the state where he operates to make sure that it is legal to include the tax in the selling price.

Although the chain-grocery and department stores make extensive use of odd prices, the variety stores have in general kept even prices on their lower-priced goods. This is shown by the popular designation of these stores as "five and ten cent stores." Various kinds of stores compete with these stores on many items. Thus, even prices are general for many articles.

Pricing at what the consumer will pay. Some retailers fix their prices on the basis of what the consumers will pay. It is necessary sometimes to sell merchandise for what it will bring regardless of what it cost. Merchandise can sometimes be sold for considerably more than it would be if it were priced by the normal markup percentage formula. This may be true of special purchases. For example, a retailer may buy a job lot and by re-sorting the merchandise can sell a portion at much more than the normal markup.

There are instances of merchandise which did not sell because the price appeared too low to the consumer. The application of the normal markup percentage yielded a price lower than the consumer desired to pay or caused him to be suspicious of quality. This may happen when a good quality product is obtained which can be sold profitably for much less than a similar product under a popular brand. Cases are known where it was necessary to raise prices several times until the price that appeared right to the consumer was found. The consumer may expect unbranded goods or private branded

products to sell cheaper than similar products under national brands. But how much cheaper? This question can be answered only by experiment. On some products it may be 5 per cent while on others it may be 25 per cent.

Prices set by manufacturers. The retail prices of some articles are suggested or fixed by the manufacturers. If the price is only suggested, the retailer is free to observe it or not as he sees fit. Some manufacturers suggest resale prices to save the retailers the trouble of computing prices and to secure some uniformity of prices in various stores.

Other manufacturers require the retailers not to sell goods for less than certain prices. Generally, only those manufacturers whose goods are widely accepted by the consumers can insist on retailers maintaining certain prices. Thus, the retailer's choice may be between observing prices fixed by the manufacturer and giving up a line that has wide consumer acceptance.

The laws in 45 states give sellers the privilege of naming minimum resale prices on their goods. A Federal law gives sellers this privilege when selling across state lines. Retailers may ignore the manufacturers' prices until sued or enjoined by a court or until the manufacturer cancels the agency. As long as the prices are in force, it is desirable to maintain them or to discontinue the handling of merchandise on which prices are maintained.

Price Lines

A large number of prices for goods of similar quality is confusing to customers. It is easier for the buyer to make a purchase if the articles are offered at only a few prices. If a woman is buying a dress, she may decide that she can pay $20. If the store offers all its dresses that would be priced near $20 at this price, the woman then makes her choice from dresses at this price. She has to decide on color, fabric, and design and the elimination of price from consideration makes her choice easier.

Many stores have found it good business to offer merchandise at only a few predetermined prices. Some chain stores have

separate buyers for each price line. Some men's clothing stores offer suits at only two or three prices. Price lining is generally used in the apparel trades. In the women's wear field this is so widely used that manufacturers make garments to be sold at only one price. Thus, one set of manufacturers make dresses to sell for $4.98; another group, to sell for $7.48; and another at $9.95, and so on. Quality is often varied in order to have the goods sold at the established price. Of course, when there are wide changes in prices as during a war or severe depression, price lines may have to be changed.

Application. One of the most widely known applications of price lining is the five and ten cent store which formerly carried goods at only two prices. Variety stores, however, have increased the number of price lines in order to broaden their offerings of merchandise. Some shoe stores have offered shoes at only one price, others at a very few prices. The same is often true of candy stores.

Price lining is used most widely in the sale of apparel—shoes, dresses, suits, coats, shirts, ties, hosiery, hats, sweaters, etc. It is often used by restaurants. It is less frequently used by hardware, grocery, and drug stores, because they sell a large variety of products that do not fall easily into a few price groups. Grocers commonly price their goods in odd cents and the prices of many articles change from day to day so that no lines can be established. However, certain products sold in drug, hardware, or grocery stores may be adapted to price lining: paint, for example, and branded lines of preserves and cookies. A store may use price lines for certain groups of merchandise even though the system is not applicable to others.

Advantages of price lines. First, price lines appeal to a great many consumers as they make buying easier. Second, they simplify the store's accounting and stockkeeping and reduce the number of errors. Third, price lines simplify the store's buying problems in trades where price lines are generally used. Fourth, they simplify the store's pricing. Fifth, they simplify marking down goods which do not sell at the marked price, as the merchandise need only be moved from one price line to another.

The appeal to the consumers is particularly important. Most

consumers have limited amounts of money to spend. Many do not like to appear to refuse to buy because of high prices. They enter stores with definite price lines knowing that they can afford the goods. They have no fear of being "traded up" unless from one price line to another. If they make their selection for a certain price line, they know the price and can devote their entire attention to selecting an article for its fit, appearance, color, design, workmanship, or materials.

Limitations of price lines. Price lining is said to have limitations in selling to the higher income consumers who want to select from a wide variety of goods and to whom price is of minor importance. It is also said not to work well among certain foreign groups who prefer to higgle over prices. As previously indicated, price lining has limited application in stores selling a great many kinds of goods and in trades where prices are constantly changing.

Price lines involve difficulties when prices change greatly and rapidly. Price lines tend to become customary prices and the latter are hard to change. When market prices change, some sellers try to maintain their established prices but vary quality up or down. Thus $14.98 dresses may vary greatly in quality, depending upon costs. When quality is lowered the reputation of a store that sells on a quality basis is hurt; consequently, the price lines may be changed instead. The difficulty in doing so depends upon the public's consciousness and acceptance of price changes. When prices advance rapidly, as during wars, the public may expect and accept changes in customary prices. At other times there are "buyers' strikes," and "boycotts."

Establishing price lines. If a retailer decides to group his goods into price lines, he must decide at what prices and at how many prices to offer goods. Determining the prices to use will depend first upon the type of customers he has or hopes to attract. Certain prices are customary in his trade and in his town. Perhaps the prices asked by suppliers limit his choice. The retailer may ascertain the prices charged by competing stores and then adopt similar prices if he wants to appeal to the same class of customers. He may adopt higher or lower prices

to appeal to a different class of customers. Or, he may find gaps in his competitors' price lines and decide to fit his prices into them. There is no simple answer to meeting, underselling, or overselling competitors' prices. The number of families in various income groups in the trade area, the number and size of stores catering to each group, and the reputations of the merchant and his competitors should also be considered. Having established oneself in a certain price class, it takes time to change the store to another price class.[1]

It has been said that apparel stores in large cities need only three price lines. In smaller cities a store may have to appeal to more income groups and so may need more price lines. A large department store may carry several price lines, but not all in one department or section. Such stores have basement prices appealing to one customer group, popular price sections appealing to another, and perhaps higher price sections for a third group. In fact, each department or section may have from three to six price lines. Too many price lines lessen or destroy the appeal of the policy.

Selection of prices. The problem of selecting price lines may be illustrated with the sale of suits by a men's clothing store. The store's sales of suits for six months are shown in Table 21–1. The store sold suits at 25 prices from $20 to $65, yet over 70 per cent of its sales were made at 6 prices—$22.50, $25, $28.50, $35, $37.50, and $45. It seems to have carried a complete assortment of sizes at the $35 price, and fairly complete assortments at $22.50, $25, $28.50, $37.50, $45, and $50. It appears that all other prices could be discarded, leaving only 7 price lines. Some of these are too close together. The store does not need prices of $25, $27.75, and $28.50. One price, probably $27.50, should be substituted for these three. Again, $35 and $37.50 are too close together and it is doubtful if both $45 and $50 are needed.

[1] A shoe chain sells three qualities of footwear. However, in one city it sells only one of these. The landlord also rents to other stores in the same block selling shoes of the other two qualities. He provided in the lease that the chain could sell only one of its three price lines. We are not necessarily endorsing the action of the landlord in dictating to his tenant; but this situation illustrates how one store can fit its merchandising plan into the local competitive situation.

Table 21–1

SALE OF SUITS BY A MEN'S CLOTHING STORE

RETAIL PRICE	NUMBER SOLD — SIZES												TOTAL SALES	
	34	35	36	37	38	39	40	42	44	46	48	50	Number	Dollars
$20.00			2		1		1						4	80.00
21.75		1	1	1									3	65.25
22.50	3	2	6	5	8	4	6	2	1				37	832.50
23.25			2	1	1								4	93.00
25.00	5	3	8	4	8	3	3	2					36	900.00
27.75		3	4	2	3	2	1	1					16	444.00
28.50	1	2	6	4	5	4	3	2					27	769.50
29.50		1	2		1								4	128.00
33.25			1	1		1							3	99.25
35.00	6	5	10	9	15	9	12	8	6	2	1	1	84	2,940.00
37.50	4	2	6	6	10	8	6	4	2	2			50	1,875.00
38.00			2		2		2	1					7	216.00
40.00		1	4	2	3	2	3	1		1			17	680.00
41.00					1		1						2	82.00
42.75			1			1							2	85.00
44.00			1		1								2	88.00
45.00	1	1	4	3	5	2	4	4	3	1			28	1,260.00
47.50			1		2		1	2	1				7	332.50
48.50			1				1						2	97.00
50.00			2	1	3		3	2	2	1	1		15	750.00
52.50			2		2			1		1			6	315.00
55.00					1		1		2				4	220.00
57.50			1						1			1	3	172.50
60.00					1								1	60.00
65.00							1						1	65.00
Total Sales	20	21	67	39	73	36	49	30	18	8	2	2	365	$12,650.00

This store might adopt the following prices: $22.50; $27.50; $37.50; and $47.50. All suits priced under $24 would be priced at $22.50; all between $24 and $30 at $27.50; all between $30 and $40.50 at $37.50; and all above $40.50 at $47.50.

Sales would then be:

48 suits @ $22.50.......	$1,080.00
83 suits @ $27.50.......	2,282.50
161 suits @ $37.50.......	6,037.50
73 suits @ $47.50.......	3,467.50
365	$12,867.50

Total sales would be increased $217.50. This, however, is not the whole story. Once the price lines are adopted, purchases would be made with these price lines in view. With fewer prices the store could do a better job of merchandising and advertising. It is probable that the number of suits sold would increase and that dollar sales would increase more than $217.50.

Markdowns

Rare is the retailer who does not have to mark down some goods from their original prices. There are several reasons for markdowns: errors in buying; decline in demand; decline in market prices; damaged or soiled goods; use of goods as leaders or specials; to meet competition; and to raise money in emergencies.

A certain amount of risk must be taken in buying and some markdowns are to be expected. This is especially true of style goods, novelties, and fads. A retailer who does not take some chances in the purchase of such goods is a poor buyer. The buyer who takes no chances has been too conservative and his store has probably lost sales by carrying limited stocks. When fashion goods or novelties do not sell within a reasonable time, they should be marked down. The general rule is that the sooner a markdown is taken, the less it will be. Some merchandising stores keep goods for only a few weeks before reducing their price. On the other hand, there are instances of goods being marked up to make them sell. Sometimes customers are skeptical of goods that appear to be worth more than the price indicates, and sales increase when prices are raised.

Consumer demand may fall off owing to a decrease in the income of the trade area or a slump in general economic conditions. When customers reduce their spending and save for a feared "rainy day," the retailer finds his goods not moving as rapidly as expected. Consequently he may reduce prices to stimulate buying.

If the prices of goods decline while they are in stock, the merchant may have to mark down his goods to meet the com-

petitors' prices, or to carry out his own policy of selling on the basis of replacement costs.

It is next to impossible to prevent some goods becoming soiled, scratched, broken, shelfworn, or overripe. Stores often have odds and ends. Such goods usually must be sold at reduced prices. Some stores selling fruits and vegetables watch their stocks closely and reduce prices promptly to prevent the accumulation of spoiled or unsalable goods.

Goods are often marked down to stimulate business in dull seasons, on dull days, or on week ends. Merchandising stores make a more or less constant use of leaders and often select goods from regular stock to be marked down. At times leader merchandise is purchased especially to attract customers.

Goods must often be marked down to meet competition. Retailers who advertise that they will not be undersold must reduce the price of any goods whenever a competitor does. Other stores make a practice of ignoring competitors' cut prices. The majority of retailers follow an intermediate course. They do not try to meet every price of every competitor but they try not to be generally undersold.

Markdown policies. It is apparent from the above discussion that markdowns are important and that the policies for handling them vary. The grocer's usual problem is to sell goods before they spoil, and to select certain goods that will attract people to his store. At times he may also have overstocks or shelfworn goods to clear out in dollar days or other special sales. The druggist often needs leaders to attract customers; he may also reduce prices to stimulate business in dull seasons or to clear out overstocks. The clothing store handles fashion goods and in normal times expects to have many markdowns to move goods that do not sell quickly. This is particularly true of women's wear.

There are two policies to follow in closing out shelfworn articles, goods that have been in stock too long, or surplus stocks. One method is to stage large clearance sales, usually at the end of the regular selling seasons in mid-winter or midsummer. When this policy is followed, shelfworn goods and overstocks are saved for the big sales. The other plan is to close

out such articles as they are found—to have a few bargains at all times. One furniture retailer put all such bargains in one place and called it a Close-Out-Corner. He advertised the merchandise regularly and customers developed the habit of looking it over.

Small price reductions, made in staple goods of known value, often result in a large increase in sales. A reduction of a few cents may double sales of a food product. A small percentage reduction may greatly increase sales of staple hardware items. In the fashion field, larger reductions are needed to convince the consumers that advertised articles are real bargains. It is hard for the consumers to judge values accurately. This is particularly true when an important element of value is fashion newness. Also they have become accustomed to larger percentage markdowns in fashion goods.

Planning markdowns. Since markdowns are both necessary and desirable, they should be planned in advance and budgeted. If records of previous markdowns have not been kept, the retailer must at first make an estimate of the amount. Some factors which must be considered in determining the amount of reduction are the volume of sales, the kind of merchandise, the stage of the business cycle, the price policy of the store, the volume of returned goods, and the promotional policy of the store. With a large volume of sales, the dollar amount of markdowns is larger. The amount of markdowns also varies with the kind of merchandise. If prices generally are declining, markdowns will usually be larger than when prices in general are rising. If it is the policy of the store to mark seasonal merchandise higher than average in the early part of the season, large markdowns late in the season may be necessary to dispose of the merchandise. Normally, the store which has a high percentage of returned sales will have a large amount of markdowns in order to sell the soiled or damaged merchandise. A store that has several promotional events during the year may have a greater amount of markdowns than the store with few special sales.

Insofar as time is concerned, the amount of markdowns may be planned or budgeted by the year, season, or month. Mark-

downs should also be budgeted by lines of merchandise or departments. It is to be emphasized that the amount of markdowns actually taken at any particular time is expected to be more than the amount planned to be taken by that time. The amount may exceed the figure allowed for that budget period. Sound merchandising must be the guide, not some budget goal which was set at a time when conditions were different. If current conditions indicate that more or less than the budgeted amount of markdowns should be made, the necessary action should be taken.

Questions

1. What general price policies may a retailer adopt?
2. What are the two meanings of the term "loss leader"?
3. *Given:* Retail $7.50; markup 40% of retail
   Find: Cost
4. *Given:* Retail $8.00; markup $3.00
   Find: Markup percentage of retail
5. *Given:* Retail $9.00; cost $6.00
   Find: Markup percentage of retail
6. *Given:* Cost $7.20; markup 40% of retail
   Find: Retail
7. *Given:* Markup $4.00 or 33 1/3% of retail
   Find: Cost
8. *Given:* Markup $5.00 or 20% of retail
   Find: Retail
9. *Given:* Retail $4.50; cost $3.00
   Find: Markup percentage of cost
10. *Given:* Cost $5.00; markup 40% of cost
    Find: Retail
11. *Given:* Markup $4.00 or 50% of cost
    Find: Retail
12. *Given:* Retail $6.00; markup 20% of cost
    Find: Cost
13. *Given:* Markup 40% of retail
    Find: Percentage of markup on cost
14. *Given:* Markup 40% of cost
    Find: Percentage of markup on retail
15. *Given:* Expenses 31.05%
    Net Profit 2%
    Markdowns 2%
    Shortages 1%
    Find: Initial markup

16. *Given:* Gross margin 32.16%
Shortages 2%
Markdowns 4%
Find: Initial markup
17. *Given:* Initial markup 40%
Markdowns 7%
Shortages 3%
Find: Maintained markup
18. *Given:* Initial markup 36%
Expenses 30%
Markdowns 3%
Shortages 1%
Find: Net profit
19. How may individual articles be priced?
20. What are the advantages of price lining? The limitations?
21. How should a retailer go about establishing price lines?
22. What are the causes of markdowns?
23. What policies may be followed in respect to markdowns?
24. How should markdowns be budgeted?
25. Should a merchant make a practice of changing the prices of goods in stock when the market prices of these goods change, that is, should he base his prices on replacement costs? Why or why not? Give arguments on both sides.
26. A store selling wearing apparel for women marks down the price of all unsold goods 25 per cent at the end of two weeks. A dress priced at $16 is marked down to $12 if it is unsold at the end of two weeks. If unsold at the end of four weeks, the price is reduced to $9. If unsold at the end of six weeks, it is reduced to $6.75. This method is continued until the dress is sold or given away. Comment on this method of making markdowns.
27. Another dealer in women's wear says that what a garment costs has nothing to do with its selling price. Once purchased, the garments must be sold for what they will bring. He therefore gets the advice of his saleswomen and marks his goods with the prices which he feels the consumers will pay for the various garments. If the garments do not sell at this price, they are marked down. Comment on this method of naming prices.
28. A dealer in men's furnishings bought a bargain lot of fancy scarfs for his Christmas trade. He priced the scarfs at $2, a very reasonable price for quick sale. At this price, they were an exceptionally good value to the consumers. They did not move at this price. As Christmas approached, the dealer became worried and marked up the price to $4. They sold

quickly at this price. Under what circumstances will a higher price increase sales?

29. Why do the margins of similar dealers vary so widely?
30. A dealer buys hats at $5 each on the following terms: 5/30, 3/60, 2/90, n/120. He pays for the hats within 30 days. What is the selling price for a markup of 40 per cent?
31. A manufacturer offers the following quantity discounts: 1-9 cases, net; 10-49 cases, 2 per cent discount; 50-99 cases, 3 per cent discount; 100-399 cases, 4 per cent discount; 400 cases (carload), 5 per cent discount and prepaid freight. Terms are 2/10, n/30. A dealer buys 400 cases and pays within 10 days. A case contains 24 items. The quoted price is $2.70 per case. What is the selling price per item for a 25 per cent markup?
32. A manufacturer quotes knives at $6 a dozen with the following discounts, 30 and 20. What is the selling price of a knife to yield the dealer a 50 per cent markup?
33. In figuring markups, the selling price frequently comes out an odd figure. Many dealers mark the price at the nearest even or customary figure. It is said that this practice causes many small losses and cuts heavily into profit, and that a dealer should use the exact odd prices. What is your opinion?
34. Bonnett's is a general store located in Graham, a town of about 2,500 population. The merchandise carried includes clothing for both men and women, furniture, children's wear, footwear, kitchen utensils, paints, radios, stoves, luggage, and refrigerators. Toys and many smaller items are also carried. Clothing includes both durable work clothes and fashion goods. The value of the stock at cost is about $35,000. The store was recently purchased by Mr. J. B. Donham, who had no previous experience in retailing. He proposes to use a single markup of 33⅓ percent on retail for all merchandise.

    Explain why or why not the merchandise should be priced as Mr. Donham proposes.
35. Elman's Meat Market is owned and operated by Mr. Albert Elman. The annual gross sales for the past ten years has been about $40,000, with a gross margin of 35 to 40 percent. Mr. Elman determines the price of merchandise on the basis of cost after deducting for loss due to fat, bones, and shrinkage. If a side of beef comes in to the store weighing 150 pounds, he figures that one-third, or fifty pounds, will be lost in fat, bones, and shrinkage, which means that he has 100 pounds to sell. If the wholesale price is 30 cents per pound, a hundred pounds will cost him $45.00 or 45 cents per pound. He generally works on a 40 to 45 percent markup on cost, which means that the sell-

ing price would be 63 cents per pound for the poorer cuts of beef and up to about 85 cents for the better cuts.

If you were the operator of this meat market, would you change the method of pricing? If so, why? If not, why not?

D. Selling

22

Sales Promotion: What It Is

THERE are many things which a retailer may do to increase his sales. What he does will vary with the size of the store and the kind of goods sold.

The Meaning and Scope of Sales Promotion

Definition. The term "sales promotion" has been used in many ways. It has been used as a synonym for advertising, but advertising has been understood to be impersonal salesmanship. Sales promotion is more than this. More synonymous with sales promotion is the term "publicity."

Sales promotion is a broad term which implies a co-ordination of many different direct and indirect methods of increasing the sale of merchandise. It is co-ordinated with personal salesmanship and is sometimes understood to include personal salesmanship. It is frequently understood to include advertising, but it includes many other methods of aiding the sale of merchandise. These methods and devices are limited only by the imagination of those who devise them.

Sales promotion, then, may be understood to include all kinds of advertising, window display, interior display, salesmanship, special sales, price leaders, and a variety of indirect selling aids or publicity methods. It includes all kinds of special sales events or "promotions." Some of these are storewide while others are used only in certain departments.

Scope. The selling viewpoint should pervade every aspect of

retail store operations and it is the responsibility of the owner or the sales promotion manager to see that it does. An owner who is disgruntled and constantly harping will develop the same characteristics in his employees and the latter will usually present the same attitude to customers.

A promotional or selling attitude should be taken by the credit department, accounting department, personnel department, adjustment department, the delivery men, buyers, porters, and other employees. Regardless of store size, whoever is responsible for the performance of this work should have the selling attitude. Every employee should have a selling attitude because of the influence of employees on each other, because customers are continually observing the relations between employees, and because many employees other than salespeople come in contact with customers.

The personnel department should handle an applicant with no less of a selling attitude than a salesman handles a customer. The applicant in the personnel department may never be employed by the store, but it is desirable that he or she patronize the store in the future. The good opinion which a prospective employee has of a store may be entirely changed by management's failure to keep up this impression after he is employed.

The credit department should use the selling attitude in handling applications for credit. The same should be true of the adjustment department and delivery men. The responsibility for developing a selling viewpoint in all employees is largely that of the store owner or the top executives.

Sales Promotion Policy and Planning

Policy. A store may have one of three promotional policies: conservative; semi-promotional, or moderately active in using special events; and promotional, or very active in various promotional events and techniques. The conservative store is usually one that is well established in the community and has a known reputation for quality merchandise. It is often an "institution" in the community. It uses few special sales and is usually relatively conservative in its advertising. The pro-

motional store sponsors many special events or stages one sale after another. Merchandising stores that make constant use of price leaders and every conceivable device to attract attention are an example. The semi-promotional stores occupy an intermediate position: more special events or sales than the conservative store but fewer than the promotional store.

The sales promotion policy will vary with the type of goods handled and the location of the store. The grocer as a rule uses week-end leaders or specials, although some stores use leaders at other times. Special sales may be used when the store finds itself overstocked, especially when prices are falling.

The filling station very frequently uses service to promote sales—for example, cleaning windshields and windows of cars, cleaning car interiors, checking and filling tires and batteries, giving road information, providing clean rest rooms, and hiring only courteous employees. Some oil refiners publicize the services available at their filling stations. One features clean rest rooms and another furnishes detailed and accurate road maps and guide books to tourists. Special services are sometimes rendered. One station in a resort town won many friends by giving tourists information on where to rent a cottage, get a boat, buy bait, find a place to fish, and so on.

Hardware stores are inclined to be the conservative type since most of their goods are nonperishable and in constant demand without special promotion. There are, however, many ways in which hardware retailers can use special promotions:

January and February—clearance sales.

Spring promotions—featuring farm and garden tools, paint, screens, cleaning supplies, wallpaper, seeds, insecticides, lawn mowers, sporting goods (baseball, golf, tennis), etc.

Summer promotions—featuring lawn mowers, hose, porch and lawn furniture, fans, thermos jugs, ice cream freezers, refrigerators, canning supplies, fishing equipment, camping equipment and vacation goods.

School opening—goods in late August and September.

Fall promotions—featuring stoves, weather strip, hot water tanks, furnaces and furnace repairs, snow shovels, corn-husking equipment, guns, ammunition and other hunting goods, football and basket ball goods.

Hallowe'en—special decorations and selected fall goods.
Christmas—toys, gift goods of all kinds.
Last week in December—clearance of toys and gift goods.

Stores handling women's apparel, men's clothing, and furniture probably make the greatest use of special promotions. Many of their goods have a fashion value and if not sold within a reasonable time they are pushed by special advertising and cut prices.

The store in a small village or in a residential neighborhood usually makes less use of special promotions than stores in central shopping districts. The neighborhood merchant often feels that there is only a limited amount of trade available, that he will get most of it, and that he cannot attract transient trade even with special sales. On the other hand, the centrally located store, although accessible to many people, depends to a large extent upon people who can be attracted to it, from other stores. Therefore it makes considerable use of promotions. The neighborhood drug store has few sales and, as a rule, seldom uses price leaders. The downtown drug store, on the other hand, often features leaders in its window displays and advertisements.

Promotions are used extensively by department stores and specialty stores selling clothing, home furnishings, and furniture. Such goods lend themselves to promotion; furthermore most of these stores are located in central shopping districts and depend on transient customers for a considerable portion of their business.

Planning. Sales promotions should be planned carefully and all the details worked out. The work includes selection of goods to be featured, preparation of advertisements for newspapers or direct mail, arrangement of store and window decorations, instructions to salespeople, and hiring extra employees if needed. Special merchandise may be purchased. In large stores plans for special promotions are often started months in advance. Sometimes plans for several promotions are underway at the same time.

An entire year's plan may be formed roughly to indicate the sale dates and goods to be featured. The Anniversary sale, the

White sale, the Post-Easter sale, the February clearance sale, Mother's Day sale, the August fur sale, and other special events may be scheduled. As the time for these special events approaches, detailed arrangements are made.

Special Sales

Special sales may be either store-wide or in only one department. Usually goods are offered at reduced prices and in normal times consumers expect price reductions. The goods may be the dealer's regular stock marked down for the sale, or they may be job lots or other goods purchased at low prices for the sale.

The objectives of special sales. A promotional event should have a clearly defined objective, otherwise the planning of the event will be done poorly. The objectives may be any of the following:

1. To build acceptance for the store's private brands.
2. To remove odds and ends from the stock.
3. To close out seasonal merchandise.
4. To build the reputation of the store as a bargain center.
5. To emphasize the store's long period of reputable service in the community.
6. To bolster a weak department.
7. To obtain new customers.
8. To increase the sales volume of regular price lines.
9. To emphasize that prices are lower than at competing stores.
10. To remind customers to buy seasonal merchandise.

It is fundamental to the success of a promotional event that salespeople, department heads, and all who assist with the planning of a special event understand the objective. This provides some assurance that all effort will have a common direction, and aids in generating enthusiasm for the event. It is difficult sometimes for the experienced employee to show much enthusiasm for a promotional event if he has participated in many of them. Nevertheless, the more fully store personnel are informed of an event, the greater are its chances of success.

Number and kind of promotional events. The number of promotional events which a store may have will depend upon its promotional policy; the non-promotional store has few or none, while the promotional store schedules one after another. When promotional events are numerous, customers tend to postpone their buying until a sale occurs. This can cause some serious problems in operation.

The variety of promotional events which a store may have is wide. Some indication of the various possibilities can be obtained from the following list:

Anniversary sale
January clearance sale
February white sale
Dollar day
Pre-Easter sale
End-of-month clearance
Department managers' sale
August fur sale
August furniture sale
February furniture sale
Baby week
Mother's Day
Father's Day
One-cent sale
Home furnishing sale
Special purchase sale
July clearance sale
Pre-inventory sale
One-hour sale
Back-to-school sale
Summer sale
Spring sale
Fall sale
Mid-season sale
Food sale
Fire sale
Holiday sales

For a store to have all these special sales would be impractical. Those which are suitable and in line with store policy should be indicated on the schedule so that proper plans for them can be made. Major difficulties in execution will be avoided if proper plans are made.

The selection of the merchandise for promotion. A fundamental task in connection with any special sale is the selection of the merchandise to be used.

First is the probable sales volume of the item or items which might be selected for the promotion. Staple merchandise may not provide the desired sales volume. It may be possible to obtain some increase in sales volume but not as much as with goods that are less staple in character. If proper records have been kept of previous promotions, a good idea of sales possibil-

ities of various items may be obtained from them. It is to be emphasized, however, that a successful promotional item at one time may fail the next time. Conditions may have changed. Some items, however, are good promotional items year after year.

The price at which a promotional item is offered has much to do with its sales volume. Merchandise with well-known prices can be offered at slight reductions and produce a sizable increase in sales volume. Larger reductions must be made on merchandise without established and well known prices.

The price at which the merchandise can be offered will bear some relation to its cost price, especially if it is purchased for the sale. Some manufacturers will not permit the retail prices of their merchandise to be cut and consequently their products cannot be featured at reduced prices. Some manufacturers will offer aid when their merchandise is selected for a special promotion. They are interested not only in helping the retailer increase his sales volume but also in securing more or new users of their merchandise. They have had numerous experiences with special promotions over a wide territory and have developed successful techniques for promoting their goods. Consequently, retailers may favor their products for special promotions.

Seasonable merchandise is particularly attractive for special promotions but the question arises—Why should goods in strong demand be promoted? The answer may be that sales volume can be further increased by giving promotional attention to such merchandise. Its price need not necessarily be reduced.

Selection of media. The publicity media selected for use during a special event will vary with the scope of the event. For an annual store-wide event lasting several days more media will be used than for a one-day event in one department. The media used will also vary with the community in which the store is located. What is practical in a metropolitan center may be very impractical in a small town. The media will also vary with the size of the store. What is suitable for the large store may not be suitable for the smaller store. Personal salesmanship, window and interior display, and some of the usual advertising media will be discussed in succeeding chapters. Some of

the more indirect methods of sales promotion will be discussed in this chapter.

Objections to special sales. Some retailers and retail executives are opposed to using the special sale. Their arguments, and an evaluation of them, follow:

1. Although special sales may boost the sales volume of the store, they increase store expenses and so cause a decrease in profits. It is difficult to determine the validity of this objection. Obviously, there is a greater expenditure for sales promotion when a special sale is held and the percentage of net profit may be less on the increased sales volume. This may not be significant since it is the total net profit which is important to the retailer. Department heads and division managers in large stores who are percentage-conscious or whose efficiency is judged by the percentage of profit necessarily think in those terms rather than of the total increase in profits. A comparison of the percentage of gross margin on goods sold during the sale is not conclusive. A good margin may be obtained on the goods bought for the sale, but large markdowns may be made on goods taken from stock. However, some of these goods might be unsalable at regular prices; the markdowns on them may be partly offset by markups on specially purchased sale goods which remain after the sale and are sold at the regular prices.

2. Special promotions do not increase the store's annual sales but only create sales peaks that are followed by valleys. It is argued that customers wait for the special sales, or that they fill their needs during the sales and buy little for some time afterward. There is truth to this objection. However, special sales are often used to increase sales during dull periods—in other words, to fill up valleys. Special sales also attract new customers, many of whom become regular customers of the store. A store must secure new patronage to stay in business, as it is constantly losing customers by removal from the community and death. As indicated on page 362, the location of the store may be an important factor in determining how many special sales will be profitable.

3. Special sales attract undesirable customers. The reduced prices may bring transient customers who are of a different class

from the store's regular clientele. Too many of these may drive away regular customers. If special sales do in fact attract customers who are not desired, the sales should not be held or should be limited in number. Perhaps they can be limited to the basement.

4. Customers who buy goods just before they are marked down may be disgruntled and trade elsewhere in the future. This is not a serious objection since most customers are familiar with sales.

5. Store service is impaired by special sales. It is necessary to employ part-time salespeople who may not have sufficient knowledge of the store system and policies as well as how to sell. A large and successful sale causes congestion in the store and places a strain on the store service. This is true of some special sales in large stores. It is not true of all special sales. Adequate planning and preparation of a special event will prevent any major impairment of store service. The personnel department of a large store is responsible for obtaining skilled part-time salespeople and other employees. Usually it maintains a file on persons who wish only part-time employment. From these records a sufficient number of people who have had the necessary previous experience in the store or elsewhere may be selected when additional employees are required.

Special Sales Promotion Methods

Some methods of promoting sales are more practical for the small retailer than for the large store. For instance, the operator of a small store frequently can make use of his ability as a contact man. An operator of a stationery and supply store, for example, is frequently seen away from his store carrying merchandise which may have been ordered by telephone. He makes a point of knowing many people and speaking with many people.

Every retailer has a civic duty. He can perform this duty by taking an active part in his Chamber of Commerce, supporting the schools, aiding with the Community Chest campaign, belonging to service clubs, and serving on various community

committees. He may not do these things with the sole object of promoting his business, but his activities will be reported in the papers. Some newspaper editors do not mention store names in their news columns unless the activity has definite news value. Most editors of small city papers will accept the story of the opening of a new store, a change in managers, or a remodeling of the building. When an anniversary sale is being conducted and considerable newspaper space is being used, the papers will often run a story about it.

Athletic teams are another indirect method of promotion. If the team members are store employees, employee morale may be helped also. This is most desirable but not always possible. The name of the store, however, appears on athletic equipment and is seen by spectators, and the results of games are reported on the sporting page. This promotion technique is of more significance to a store that sells merchandise bought by men than to one selling merchandise bought by women.

Contests are another method of indirectly promoting the store and its merchandise. A needlework contest provides attractive materials for window displays and makes a special appeal to women interested in knitting, crocheting, weaving, and sewing. Photographic contests draw attention to that line of merchandise. Pet contests attract crowds and call attention to the food and other requirements of pets. Some retailers are opposed to the use of contests unless every contestant can be a winner. They believe that ill will is created unless everybody wins.

The fashion show is a promotional device which has been frequently used by large stores. The small clothing retailer often believes that he cannot stage such a show because he is too specialized. However, several small retailers may coöperate in presenting one. Unless one or more of the retailers possesses real showmanship and is willing to "produce" the show, perhaps other methods of sales promotion should be used.

Demonstrations of merchandise inside the store or in the windows attract attention and draw crowds. Cosmetics and household appliances, for example, are frequently demonstrated by a manufacturer's trained representative. A better than the

average retail salesman may do the demonstrating if one is not available from a manufacturer.

So-called schools of instruction aid indirectly if not directly in the sale of merchandise. Those receiving the training in knitting and cooking, for example, are required to buy the necessary materials in the store.

The large store may make use of the visits of authors, athletes, actors, actresses, and other professional and semiprofessional people to attract attention to different lines of merchandise. Even some smaller specialty stores have successfully used such visitors.

To "produce" a promotional event on a store-wide scale the various appropriate direct and indirect methods of selling must be selected, scheduled, co-ordinated, and set in motion.

The Sales Promotion Budget

How much to spend for sales promotion depends on several factors. The first of these obviously is the policy of the store. A promotional store will spend more than a non-promotional store. A store which handles primarily nationally advertised brands may spend less of its own money than a store with no brand policy. Brand manufacturers do much of the promotion and furnish retailers with promotional material.

The size of the store and the nature of the merchandise handled will also determine the amount spent. A small store handling primarily convenience goods will spend relatively little on sales promotion.

The competitive situation is another factor. If competition is intense or if competitors are strongly promotional-minded, the fact cannot be ignored. To do so may mean a decline in sales.

Expected business conditions also have a bearing on the amount to be spent for increasing sales. When sales are falling because of a general decline in prices and consumer income, the sales promotion budget allowance is often reduced. This may be desirable if most competitors reduce their expenditures. On the other hand, some merchants argue that the promotional expenditure should be increased to boost sales or at least to

limit their decline. When prices and consumer incomes are increasing, a larger amount is usually spent for promotion in order to make sales increase faster than they would otherwise. It is easier to build sales volume when the customers have the money and are in a buying mood than at other times. It is much easier to row with the current than against it. The merchant who increases his promotional budget in dull periods in order to get a larger share of the community's business may not expect to increase his expenditures when business is on the upswing. When business is improving he may feel that his sales will increase anyway and so ease up a little on his expenditures for special promotions.

There are several ways of determining the amount to be spent on advertising and other special promotional methods. Perhaps the most widely used method is to base the budget allotment on either past or anticipated sales. Thus, a given percentage of sales is set aside for promotion. If this percentage is based on past sales, it often happens that promotion expenditures are decreased when they should be increased and vice versa. It is therefore better to base the budget on the sales anticipated for the coming period.

A better method of determining the amount to be spent on promotion is to consider the goal to be achieved—the objective of the promotion. A store may have a long-term objective: improving the store's reputation in the community for carrying complete stocks of quality merchandise. Expenditures for this objective will extend over many budget periods. Meanwhile, the immediate objective may be the sale of a specially purchased lot of goods. The problem is to determine how much it will cost to put the sale over. Another objective may be to increase sales in a specified department to a definite figure (say $100,000) during the coming year. The problem is how to secure this sales volume and to appropriate the money necessary to carry out the promotion.

It may be good policy to promote sales of weak departments. Often a store has a high reputation for one department and a mediocre reputation for its other departments. One store may be known for its shoe department, another for its linens, an-

other for its furs, another for its dresses, another for its sporting goods, and so on. Perhaps a store finds that many of its dresses are sold to women who go elsewhere for their shoes. Some stores analyze purchases made by individual customers and find that many do not patronize all departments of a store.

A store, for example, may find that its shoe department is weak competitively. In order to improve its reputation and sales, it may be necessary to study the various operations. Perhaps the buyer is too conservative. Perhaps the stock is incomplete in styles, price lines, sizes, and lasts. The obvious course is to buy and carry more complete lines. However, if more shoes are purchased and sales efforts not increased, large cut-price clearance sales may be necessary. When the stocks have been built up, sales efforts must be increased. One method is to instruct the salespeople in other departments to request their customers to visit the store's shoe department. These salespeople may do much to spread the news that the store has one of the largest and best stocks of shoes in town.[1] Direct-mail advertising may be sent to store customers who buy their shoes elsewhere. Form letters, personal letters, printed booklets, or folders may be used. The next step is to improve the salesmanship in the shoe department. More window space may be allocated to shoes. Then all of these efforts may be supported by increased newspaper and/or radio advertising.

Building up a weak department is a definite objective and the estimated amount needed to do the job must be provided.

A third method of determining the amount to be spent on promotions is the profit earned on various goods. A widely known firm of management engineers determines the profits on various products of its clients, and then recommends that they increase their advertising and selling expenditures on the more profitable lines. The retailer similarly may determine his profit on various lines or commodities handled and increase his sales efforts accordingly. This is said to offer one of the most practical methods of increasing a store's profits.

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[1] Study of customer purchases by lines or departments and attempts to induce customers to patronize all departments in a store has been called "customer control."

The amount to be spent must be distributed among the media to be used—newspapers, direct-mail advertising, outdoor advertising, store decorations, window displays, radio announcements, and the like. From available media, the problem is to select those that are best adapted to the job and that will secure the desired results at lowest cost.

The appropriation is also distributed according to the dates of the promotion events. There should be some flexibility in the budget. To illustrate: a promotion on fishermen's equipment may be scheduled for the opening of the fishing season. However, if sales are less than expected, an additional appropriation may be needed to promote the sale of these goods at reduced prices before the season closes.

Questions

1. What is meant by the term "sales promotion"?
2. Is the responsibility for promoting sales entirely the responsibility of the sales promotion division? If not, how can other departments assist?
3. What three sales promotion policies may be adopted?
4. What should a sales promotion plan include?
5. What may be the objectives of a promotional event?
6. What are some of the various kinds of promotional events which a store may have?
7. What should be considered in selecting merchandise for special promotion?
8. What are the objections to special sales?
9. What are some of the sales promotion devices or methods used by the small retailer? By the large store?
10. Are contests a satisfactory method of promoting sales?
11. What determines the amount to be spent for sales promotion?
12. How may this amount be determined?

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Effective Advertising

ADVERTISING has been defined as "salesmanship in print." A somewhat more technical definition which includes radio advertising is: "Any paid-for form of non-personal presentation of facts about goods, services, or ideas to a group."

Probably most retailers advertise to increase their sales. There may, however, be other reasons such as: to reduce other operating expenses; to sell the store as an institution in the community; to build confidence in the store and its goods; to sell the idea of the quality of the store's merchandise; to increase the rate of stock turnover, reduce expenses and increase profit; to attract new customers; and to extend the store's trading area. The ultimate objective is to increase the store's profit either in the immediate future, or to increase or stabilize profits over a longer future period.

Advertising Media

The various types of advertising media may be enumerated as follows:

Newspapers
Magazines
Radio
Outdoor posters and signs
Road signs
Shopping news
Car cards
Telephone directories
Direct mail
Movie trailers and slides
Handbills
Calendars
Programs
Store papers
Souvenirs and novelties
Premiums
Manufacturers' folders and inserts
Catalogs
Selling and service literature

Few stores are in a position to use all the media listed above. The most widely used are: newspapers, direct mail, handbills, posters, programs, radio, and manufacturers' folders and inserts.

Newspapers. The newspaper is one of the best media. The small retailer, however, can seldom economically advertise in a metropolitan daily. He would be paying for too much circulation to readers who are outside his trade area. The store in the central shopping district can use the metropolitan paper if it is large enough to attract enough customers to make this a profitable medium.

The chain with a number of stores in one city may find the metropolitan daily a profitable medium in which to advertise. Independent retailers who are members of a buying club or a coöperative or voluntary chain may also use the large city dailies. To do so usually means that they must buy together so that each store will have the advertised goods at the advertised prices. If the stores are operated under the same name, they may run an ad featuring their services or the quality of their goods. The usual retail advertisement, however, features selected articles at named prices. There are many neighborhood papers published in metropolitan areas which neighborhood and suburban stores may use.

The store in the country town usually can use the weekly paper in its trade area advantageously. Likewise the store in the small city may be able to use the daily paper. The stores in such locations can probably use newspaper advertising to better advantage than can stores in other locations. Want ads may prove an excellent medium for selling used articles such as trade-ins and repossessed goods.

Shopping news. In some cities papers termed "shopping news" because they contain principally advertisements are published. Large stores in the central shopping area may sponsor them because they are a lower-priced medium than the daily papers. If distribution is city-wide, it is hardly suitable for a small or neighborhood store; but if its distribution is confined to a neighborhood trading area, it may be an economical medium. In many respects a shopping news resembles a neighborhood newspaper. Although neighborhood shopping news

may not be read as carefully as the regular news dailies, it sometimes is the most practical advertising medium for the neighborhood retailer.

Direct mail. Direct-mail advertising can be used by almost every store. It consists of letters, circulars, booklets, catalogs, post cards, merchandise samples or other materials that can be sent through the mail. The mailing may be prepared by the retailer, by the jobber, or by the manufacturer.

The message may feature leaders, or call attention to special sales or to seasonable goods. Stencilled mailings may be illustrated by cartoons, charts, or diagrams or by small photographs bought in quantity and pasted on the letter. If the letter is printed, halftones may be used.

Circulars and handbills usually feature definite articles at named prices. If used only occasionally they usually call attention to some leaders offered at low prices. The retailer who sends out handbills regularly can use them for almost any type of advertising.

Catalogs or folders are often supplied by jobbers. For example, some buying brokers have such booklets printed by the million. They put out an advance list of items and star those to be shown in the proposed booklet. The jobbers show this list to the retailers and sell them on its use. The retailer who decides to obtain the booklet must buy the starred items, but purchase of the other items is optional. Many of the items listed by the jobber are bought in large lots from the manufacturers at off-season low prices. The resultant low cost to the retailer enables him to sell the merchandise at attractive retail prices. These booklets bearing the retailer's name and address are used most often for Christmas or other seasonal goods. Frequently the retailer turns over his mailing list to the broker who has the booklets mailed to the retailer's customers. These booklets appear to be an excellent medium but their usefulness is limited by the infrequency of issue.

Postcards may carry the prices of the store's specials or may feature a single article. Cards for the latter may be furnished by the manufacturer with space for the dealer's name. The dealer may also send out leaflets or booklets supplied by the

manufacturer and featuring his line with the dealer's name and address imprinted.

Direct-mail advertising can be very effective. When it is not, the reason is probably the infrequency of its use, its poor quality, or an inadequate mailing list. Like any other advertising, direct mail, to be effective, should be continuous and should be well done. The retailer can probably put more of his personality into direct mail than any other form of advertising, with the possible exception of radio.

The mailing list is important to the success of direct-mail advertising. No matter how good the copy is, or how attractively it is printed, it will not be effective if it does not reach the prospective buyers. Mailing lists for people in a town or small city may be made up from: names of credit customers; names in telephone and city directories; membership lists of churches, clubs, and the like; lists of property owners and taxpayers. After a list is built it should be kept up-to-date by removing the names of families who move away and people who die and adding the names of newcomers.

Retailers in a town may exchange mailing lists or they may coöperate in having a list constructed and kept up-to-date. A retailer may secure names and addresses of cash customers by having his salesmen request this information when making routine sales, or during a special sales event. An advertisement offering a free gift or a special inducement such as a contest with prizes, and requiring the name and address on a coupon will secure new customer leads. The retailer in the large city has a more difficult task in building a good mailing list than does the dealer in a small town. Telephone and city directories are usually alphabetically arranged, and in a large city it is a big task to pick out the names of the people in his trade area.

Mailing lists may be purchased but such lists are unlikely to be suited to neighborhood retailers. For a local area they are likely to be obtained from city or telephone directories and they may not be kept up to date. It may, however, be more economical to buy a copy of a list than to make up a list from local directories.

Handbills. These are usually delivered from house to house

by carrier. A high percentage of them are not read. They are most often used to announce a special, or seasonal goods, or a new line added to the stock. If the retailer is located where he can have his bills delivered properly and if he will use them regularly, he can make them a useful medium.

Programs. Programs for sporting events, theaters, and other entertainment are a common form of advertising for stores in the smaller towns. They usually carry little besides the retailer's name, slogans, and a few lines about the kind of goods sold. This is known as institutional advertising. Because program advertising is often done for its goodwill value rather than for any immediate increase in sales, it is difficult to judge its worth. Some retailers consider program advertising more of a donation than advertising.

Novelties. Such articles as yardsticks, rulers, calendars, or blotters bearing the store name are considered a good advertising medium by many stores.

Radio. Radio, like newspapers, is widely used by large stores but is seldom available to the small store in the large city. Many of the smaller cities and towns, however, have local stations which are used by local retailers. The station may have a staff that will prepare the commercial for the store and supply the music, news, or the type of program wanted by the store. Because radio advertising can be very effective, the retailer should consider carefully the benefits of using a station that covers his trade area at a reasonable cost.

Movie slides. Small-town and neighborhood movie theaters often run trailers or slides. This form of advertising is a good way of reaching potential customers, although it may be a rather costly medium. Trailers or slides usually carry a message about the service rendered by the store or simply the store's name, address, and quality of goods handled.

Manufacturers' folders and leaflets. Such materials are usually excellent advertisements of the manufacturer's product or line. They are often inserted in the monthly bills and statements. If these folders advertise an important product or line, the retailer may secure and distribute them himself, or furnish his mailing list to the manufacturer who will mail them out

with the retailer's imprint. If such folders feature only a relatively unimportant product, the retailer may not be enthusiastic about their use. It is to the retailer's interest to build up his store and not spend too much time and effort in pushing a single product, unless it may become a large-volume product.

Premiums. Premiums can be used very successfully to introduce new products and increase the sale of old products. The idea of "something free," or "something for nothing," appeals to most people. Some companies without funds for large advertising campaigns have used premiums successfully. Retailers often distribute premiums and free goods for manufacturers. Few, if any, small stores have introduced their own premiums.

Advertising Copy

Types of copy. There are several types of copy: price, quality, factual, service, reminder, and institutional. It may appear in many forms.

Price. Price advertising is a very common form of retail advertising. It is the type usually used by retail food stores. It frequently takes the form of listing products of known quality or value at attractive prices. A low price for a product of unknown value is meaningless to the readers. Thus price advertising usually takes the form of announcing the store's leaders or products on special sale.

Quality. This widely used form of advertising has helped to establish the reputations of some stores as vendors of quality merchandise. On the other hand, it sometimes has created the impression that the store's prices were high. If a retailer constantly advertises "highest quality goods," or "we sell the best quality of merchandise," the readers may come to believe that he does but they also infer that his prices are high. He cannot mention price in general unless he says "at reasonable prices," or "at low prices." If he says "highest quality and lowest prices," readers are likely to be skeptical. This indicates that the retailer should use a carefully planned program of both quality and price advertising.

Factual. Factual ads mention the price and also give specific

information about a product—its use, construction, or performance. The dealer thus combines quality and price advertising. Information for such ads may be obtained from the manufacturers.

Service. Some retailers advertise their services—delivery, credit, repair, or their general willingness to serve. It may take the form: "If we don't have it we will gladly get it for you," or, "We are glad to explain our goods and you are under no obligation to buy. Come in and give us a try." The retailer who advertises such service should give service. His advertisements should not be an empty boast. Advertising to be effective must be true.

Reminder. Some stores are in an excellent position to use reminder copy. "Cold wave coming, do you have enough antifreeze?" "Blizzard on the way, do you need a snow shovel?" "The bugs are getting busy, have you sprayed your garden?" "Spring is here, that wall paper should be cleaned!" "Winter is on the way. Have you weatherstripped all your doors and windows?" "It's picnic time. Do you have a thermos jug for that hurriedly planned picnic? We also have a complete stock of paper plates, cups, spoons, and other picnic accessories."

Institutional. Institutional advertising is intended to keep the name of the store before the public and to build goodwill. Advertisements on programs, on theater curtains, and in baseball parks are only three of the many forms of institutional advertising. It may give new information about the construction or use of products. For example, one advertisement might tell of the invention and development of the gasoline engine, another of the diesel engine, another of the invention of the mechanical reaper, and so on. Such a series may be widely read because of their interesting information. The retailer's signature at the bottom keeps his name before the public.

Preparation of copy. Copy writing is important, yet it is done poorly by many retailers. The amount of time devoted to other problems and/or the lack of ability to prepare good copy are two reasons why their copy is unsuccessful. So many problems call for the retailer's attention that he does not take the time to plan and prepare good copy. He must (1) plan and arrange

window and store displays; (2) keep stock and buy goods; (3) sell goods and supervise salesmen; (4) hire and train new employees; (5) adjust customer complaints; (6) see that his store is kept clean, properly lighted, and heated; and (7) do the many other things involved in successful store operation. The result is that advertising is often neglected; either it is not done at all or it is done in a slipshod manner.

What can the retailer do when he lacks the time and ability to plan and write good advertising? There are several possibilities. He may find that one of the employees has the interest and the necessary ability. The local paper or radio station may be willing to prepare his advertising. In some cases this may be a satisfactory solution, but in others it will not, because the advertising, though grammatically correct, will be trite and fail to express the personality of the store. Another solution is to employ an outsider to write the advertising: a newspaper reporter, the advertising manager of a non-competing store, or someone else who has the ability to write good selling copy.

The retailer who belongs to a voluntary or coöperative chain may use the copy prepared by this organization's advertising department. In this way several retailers combine to pay for competent advertising service.

The retailer may buy the service of a professional advertising service company. Such a service may furnish cuts or mats for the advertisements. Such material may be satisfactory as is, or it may be advisable for the retailer to modify it to suit his special requirements.

If all these methods are impractical, perhaps the retailer had best secure a location with high traffic density and depend very largely on his window displays to draw people into his store. His advertising can be limited to the occasional use of newspaper ads, direct-mail pieces, and materials supplied by jobbers and manufacturers.

Planning copy. The advertising may be made distinctive by the proper selection of a type face and border, or by a regular and definite location in the paper so that the readers come to recognize and look for it. A store may adopt and feature a slogan which identifies it with the public and gives it distinction.

Examples are: "The store where Quality Reigns and Shopping is Pleasant," "The Bargain Corner," "The Quality Store where Parking is Easy," "Blank's has Everything for the Home."

Color attracts attention and is very important. Color is used occasionally in newspaper advertising but the printing production difficulties involved have, to date, limited its use. It should be used whenever practical in direct-mail advertising.

One illustration is worth many words. Owing to the coarse screen required in newspaper printing, the reproduction of photographs is not always satisfactory. Their use in other forms of advertising increases the cost since a good grade of paper must be used. The results, however, often justify the expense. The retailer may use photographs of the products, the customers, the product in use by customers, or line cuts—for example, cartoons and diagrams of the merchandise. Most illustrations usually show the products.

Layout is an important part of copy writing. The following are questions concerning layout: How much white space? What size type? Where should cuts be placed? How much text should the advertisement have? The casual reader often sees only the headline and the illustration and must be led from there into the text. Too often the body of the ad is not read; so the text should be as short as possible. Yet in a factual ad there must be text material. To attract more readers, the text should be condensed, the facts specific, the adjectives well chosen. A sufficient number of carefully selected illustrations will attract attention to the various articles featured in the body of the advertisement, help to keep the text as brief as possible, and still make an effective ad.

The headline is, perhaps, the most important part of an advertisement. Certainly it and the illustrations are the most important part. They must attract attention and arouse interest. If they do, the body of the advertisement may be read. They may by themselves attract people to the store. Composing a good headline may take as much time as writing the rest of the advertisement. A good headline attracts attention and gives the main point of the message. It may be bargains, new merchandise, scarce merchandise, the use of goods, the saving in-

volved in a purchase, or what the product will do. "Save 10 per cent on your coal bill" (stoker). "Time for Play" (slacks). "Get the Higher Price for Grade A Milk" (sterilizing equipment). "Hot Water Always on Tap" (hot water heater). "Vitamins Are Healthy. Keep Them in Your Food" (cooker), or "Guard Your Children's Health, Keep the Vitamins in."

Appeal to buying motives. The advertisement, like the salesman, should appeal to one or more buying motives. The copy writer should constantly ask himself: "To what motive does this appeal?" A picture shows a small, neatly dressed woman with a big scoop in her hand standing between a huge pile of black coal and the open furnace door. The headline is: "Does your wife have to do this while you are away?" This appeal to affection may sell more stokers than the saving in cost of fuel. Other appeals would be health and comfort resulting from an even temperature in the home. A picture of a housewife reading a book and the hands of the clock pointing to 11 A.M. with a headline "Washing Done at 11 o'clock; Plenty of Time for Reading" may sell more washing machines than calling attention to the labor saved in rubbing clothes. It suggests how the extra time may be used. Any number of product uses can be shown, for example: "Enjoy Delicious Frozen Desserts," with a picture of the refrigerator and the delicious dessert being taken out by the housewife.

Manufacturer's copy. Manufacturers often supply copy featuring their products. Some feature in it the store's products and include their own. In some cases, the manufacturer pays part of the cost of newspaper advertisements for his products. The local retailer can purchase space for his own advertisements at the local newspaper rate, which is usually considerably lower than the paper's national rates. If the product is one of major importance to the retailer, he may coöperate with the manufacturer to their mutual profit. The retailer should not, however, adopt every such plan simply because the manufacturer will pay part of its cost. He should ask: Do I want to feature this product? Is the copy suited to my territory and my customers?

Location. A newspaper advertisement in a good location will

be read by more people than one in a poor location. The upper left-hand corner of a page surrounded by reading matter is a preferred location but few papers allot it to advertising space. Bottom of page on left-hand side or in center with reading matter above is a good space and more often obtainable. The back page of the paper is preferred by some advertisers. The upper right-hand side of page alongside the reading matter is also a preferred space. The product advertised may affect the location desired for it. An advertisement featuring housewares will probably draw better on the "Woman's Page" than on the "Sporting Page."

Some papers will give preferred locations for an additional charge, or for long-term contracts calling for weekly or daily insertions. If so, the dealer must decide if the location is worth its price. It may be, if the store advertises regularly and the extra cost is not too great.

It has been proven time and time again that advertising can be successful and profitable. This does not mean that all advertising is profitable. We have indicated some of the factors needed for good advertising: Media suited to the product and the customers; a properly selected appeal; and well-written copy, especially headlines and illustrations. In addition, to be effective, advertising must be more or less continuous. The retailer may use the newspaper, the radio, a store paper, direct mail, or handbills; or he may use several of these. Whatever media he selects, however, he should use regularly.

Planning the Advertising

The proper planning of advertising includes the merchandise to be featured in the store's advertising, in the store's windows, and in the inside displays. Each of these should be planned by seasons. Some stores prepare a calendar showing for each week in the year the goods to feature in the store's advertising and windows. There will need to be some flexibility in applying the plan in order to allow for goods which sell better than anticipated, or in which the store is overstocked. The plan will of course influence the store's buying. If an article is to be pro-

moted, the store should have a sufficient quantity on hand to care for the demand.

The retailer must, of course, have general supervision of the plan but he may turn its preparation over to an employee, perhaps the one who prepares his advertising.

It will help in this planning if he keeps a scrap book or idea file containing copies of his own advertising and of other advertisements clipped from newspapers and magazines. Notes jotted down from time to time can be filed for future use. The collected material will help in planning advertisements and avoid the necessity of hastily throwing something together to meet a deadline.

New information is at first forgotten rapidly and later more gradually. A new store or a new product should use a large space frequently until it has impressed itself on consumers' minds and then it may use a smaller space less frequently. Thus, an established store may advertise regularly—perhaps once a week—in the local paper and if possible in the same space.

Another principle of timing is to advertise when the goods are in greatest demand. This is based on the belief that best time to advertise is when people are in the buying mood. Paint may be advertised in the spring and summer, house cleaning supplies in the spring, picnic supplies in the spring and summer, skates and sleds at Christmas time, canning supplies in the summer and fall, screen wire in the spring, and so on.

The advertising expenditure. One retailer may elect to pay a high rent to secure a location on a street with a high traffic density. Another retailer may elect to pay less rent for a location with less traffic and then spend more for advertising to attract customers to his store. Either policy may be successful. Generally, the store that sells principally large articles such as household appliances and furniture and the like may select a location with lower rent and depend on advertising or outside selling to secure the desired sales volume. On the other hand, a store specializing in variety merchandise, drugs, dresses, shoes, china, gifts, toys, and similar goods is more likely to pay the higher rent for the higher-traffic location and depend more on its windows to attract customers. Thus, there may be a direct

relation between a store's location and its advertising expenditures.

The amount spent for advertising varies considerably from store to store. Some stores spend about 1 per cent of sales. On this basis, a store with $30,000 sales spends $300 for advertising while a store with $100,000 sales spends $1,000 for advertising. These are not large amounts and it may be that most stores should spend more. The merchandising store spends considerably more than does the non-promotional store. The retailer should try to plan his advertising in a way to secure the maximum results from his expenditures. To do this he should budget his advertising expenditures carefully.

In making up his advertising budget, he should plan his advertising expenses by the year, season, quarter, or month. The amounts should be broken down according to the media to be used: so much for newspapers, so much for direct mail, and so much for radio.

Donations and gifts should not be charged to the advertising budget. These average between 0.1 and 0.2 per cent of sales for some stores. The contributions are made to groups such as the Community Chest, the Y.M.C.A., Y.W.C.A., Red Cross, high school band, boys' clubs, Christmas party for underprivileged children, and so forth. In addition to such gifts charged to the store, the owner usually makes additional gifts to religious and charitable organizations.

The advertising budget. The small retailer should prepare an advertising budget. The following will illustrate the method. Let us assume that the retailer is located in a small town with a weekly paper, that he decides to spend $800 on advertising, and selects newspaper and direct mail as his media. He will prepare the copy with the help of the newspaper so that no part of the appropriation need be set aside for copy preparation. We will assume also that the newspaper provides a mat service and a supply of cuts from which the retailer can select some part of his illustrations at no extra cost. Many cuts and mats will also be supplied by the product manufacturers.

The paper, published weekly, has a local advertising rate of 25¢ per inch. A ten-inch two-column ad would cost $5.00.

However, if the retailer will agree to advertise each week during the year, the rate will be 20¢ or $4.00 for a two-column ten-inch ad. He may or may not accept this rate. Let us suppose he does. His regular advertisements for the 52 weeks in the year will cost him $208. He then plans to spend $290 for additional newspaper space for his spring, summer, fall sales and for January-February specials to clear up dead stock. For his Christmas trade he will use a booklet bought through his jobber. He will also use direct-mail pieces for seasonal goods, and for his mid-winter specials. His total direct-mail appropriation is $249.

His advertising plan would look like this:

Newspaper advertising:		
Regular weekly advertisement	$208	
Larger advertisements for January-February clearances	30	
Larger advertisements for spring goods	120	
Larger advertisements for summer goods	60	
Larger advertisements for fall and winter goods	80	
Total newspaper		$498
Direct Mail:		
Spring goods	$ 50	
Summer goods	30	
Fall goods	45	
Christmas goods	75	
January clearances	25	
Extra help in addressing	24	
Total		$249
Extra cuts and mats	20	
Programs and school papers	33	
Total		$ 53
Total advertising budget		$800

His regular weekly advertisement will be used for institutional advertising to keep the name of the store before the public and to build goodwill, reminding the public of their need for seasonal goods, and calling attention to specials and new merchandise. His direct-mail advertisements will be larger and primarily factual, describing goods and giving prices. They will be as fully illustrated as is practicable.

A smaller store with a budget of $400 might omit the regular weekly advertisements and reduce the number and size of the seasonal goods and the direct-mail advertisements. It would likely have a somewhat smaller mailing list. Other stores might vary the media used. A neighborhood store in a large city, for example, might spend most of its advertising money on direct mail, handbills, theater slides in the neighborhood theater, and outdoor signs. Another neighborhood store might substitute advertisements in the neighborhood paper for direct-mail advertisements. A village store may issue its own store paper. A store in a small city with a local daily might spend practically all its money for newspaper advertising while another might spend most of its money on radio advertising. The downtown store in the large city may use newspaper advertising or it can build a mailing list and use direct-mail matter. Regardless of the location, however, the retailer should plan his advertising carefully, and this plan means a budget.

Questions

1. Distinguish between the terms "sales promotion" and "advertising."
2. What are the objectives of advertising?
3. Can the small retailer located in a large city profitably advertise in a metropolitan daily newspaper? Why or why not?
4. What advertising media are practical for the small retailer?
5. What are the various types of advertising copy? Explain each.
6. What assistance is available to the small retailer in preparing his advertising copy?
7. What are the most important parts of an advertisement? Why?
8. What questions should the retailer ask in determining whether or not to use copy furnished by a manufacturer?
9. What are the preferred locations for an advertisement?
10. What factors contribute to the effectiveness of advertising?
11. How should advertising be planned?
12. How should the retailer determine the amount to be spent for advertising?
13. What types of radio programs are most popular? What percentage of the time in radio programs should be devoted to advertising and how much to entertainment?
14. It is said that direct-mail advertising is scientific, or can be made so. What is meant by this statement? Do you agree?

15. Can successful advertisements be based on fear? Select "fear" advertisements from current periodicals and tell which you think are good and which you think are bad.
16. Make a list of the chief buying motives and select two advertisements from current periodicals that appeal to each motive. (Paste each advertisement on a sheet of paper and write the appeal below and hand in.)
17. What appeals would you use in advertising the following products: metal furniture for the home? pre-fabricated houses? pancake flour? railroad passenger service? bonds? garden seeds? ice cream? milk? computing machines? farm implements?
18. Select advertisements illustrating institutional, product, and price advertising. (Paste on paper and hand in as suggested in Question 16 above.)
19. Clip advertisements from current newspapers or magazines illustrating a good use and a poor use of each of the following: layout; illustration; color; headline; copy.
20. Prepare the copy and make the layout for the following advertisements to appear in newspapers:
    (*a*) A new arrival of fashionable men's oxfords to be sold at $9.50. (Size: 2 columns by 9 inches.)
    (*b*) Baseball equipment to appear in the early spring. (Size: one quarter page.)
    (*c*) Fishing tackle and supplies to appear during the summer vacation. (Size: 27 column inches.)
    (*d*) A clearance sale of ladies' winter coats, marked down from $45 to $32.50. (Size: not to exceed one-half page.)
    (*e*) Electric fans. Ad to be prepared in advance and run during the first heat wave of summer. (size: 2 columns by 6 inches.)
    (*f*) A special sale of ladies' dresses, special value on a new purchase, to be sold at $17.50. (Size: one-quarter page, any shape.)
    (*g*) A spring ad of seeds and garden supplies, to appear in a small-town paper. (Size: not to exceed 28 column inches.)
21. Prepare direct-mail advertising for the following products:
    (*a*) A leather handbag at $7.95.
    (*b*) Real old-fashioned hickory-smoked Virginia hams, cured and offered for sale by a farmer in Virginia.
    (*c*) Genuine Vermont maple syrup offered for sale by an association of producers.
    (*d*) Saturday specials of a neighborhood grocery store.
22. What position in a daily newspaper would you want for an ad offering a cookbook for sale? What position would you want for an ad of golf clubs? For an ad of groceries?

24

Window Display

WINDOW displays are of major importance to most stores. Many stores depend primarily upon their window displays to attract customers into their stores.

The windows are the most valuable single part of a store. If it is estimated that a display window is worth $1.11 per 1,000 people passing by; and if the window is passed by 16,000 people, it would be worth an average of $17.76 per day.

Some estimate a window to be worth from 3 to 10 cents per square foot per day according to the density of passing traffic. If this computation is used, a window 5 by 7 feet is worth from $1.05 to $3.50 per day depending on the traffic, while a window 8 by 12 feet is worth from $2.88 to $9.60 per day depending on the traffic density.

Some assign from one-sixth to one-fourth the value of the first floor to the windows, depending on the size of the windows and the depth of the store sales room. If a retailer pays $180 a month rent for his room, the display windows are worth from $30 to $45 per month.

By any of these methods, it is obvious that windows are valuable and that the success of the retailer depends in no small measure on the quality of his window displays.

Object of Window Displays

Window displays have three objects: to attract attention, to arouse desire, and to draw people into the store.

Attracting attention. Attention may be secured by a display of merchandise, by movement, color, light, sound, novelty, demonstration, and spectacles or stunts. Many articles of merchandise are of unusual interest in themselves. They will usually secure attention when they are displayed in the window.

People are attracted by movement. The following will illustrate the possibilities: Electric trains; a waterfall—the water is pumped by an electric motor and a boy may be shown fishing below the falls; machines in motion—a revolving wheel may carry various messages on its panels (perhaps in different colors); pictures ("stills") rotated by a mechanical device, or moving pictures projected on a screen. Mechanical devices showing dummies or marionettes in motion seldom fail to attract the attention of passers-by.

Color may be used to attract attention. Vivid backgrounds or pictures may be used or brightly colored goods may be displayed in the window.

The best-lighted window attracts the most attention, other things being equal. Light and color are often combined. Novel displays are excellent for attracting attention.

Window demonstrations may be staged to show the performance, operation or use of a certain article. Demonstrations are good attention-getters, partly because of their motion. They usually carry a sales appeal for goods sold by the store. For example, a stream of water may be kept flowing over a raincoat, a tent, or a piece of tarpaulin to show that they are waterproof, or over some other article to show that it is not damaged by water. Or a woman may operate a sewing machine and talk through a microphone and loudspeaker to the people on the sidewalk.

Sound attracts attention, too. The old tick-tack device served the purpose of making people look at the window. Music may be supplied from records, a radio may be kept tuned in, or a loudspeaker may carry a message. At times when some exciting news event is on the air (an outstanding athletic event, for example) the radio may secure much attention. Sound depends to a large extent upon its novelty.

Some retailers make use of many spectacle or stunt exhibits.

The boy fishing below the waterfall is one example. At Hallowe'en a shock of corn, pumpkins, autumn leaves, and witches on brooms may be used. Some of the store's goods may be used in the exhibit. Other seasonal themes include: a hunting scene showing the hunter (with dog and gun) firing at birds; Santa Claus, with his reindeer and a pack of toys; George Washington cutting down the cherry tree. A scene showing Lincoln splitting rails might include a display of axes, mallets, saws, chains and the like. A display of fishing equipment might feature a scale model of fishermen, tents, boats, or the prize specimens caught last year. The retailer may arrange elaborate displays that show his merchandise. He can, for example, show the June bride and groom before the altar as a setting for a display of wedding gifts obtainable from his store.

Another type of novel display would be a window showing pictures of the town at the time the store was started. Other examples are window displays of war trophies, old firearms, or trophies to be given in the golf tournament or at the county fair.

Drawing people into the store. People may have their desire for the displayed goods aroused by the window display and come back later to purchase. The immediate object of a window display, however, is to attract people into the store. Many of the spectacular and stunt windows are wonderful attention-getters but of relatively little value in drawing people into the store. Unless spectacle displays draw people into the store, their number should be limited. Such displays, however, may call attention to the store and thus serve as institutional advertising or goodwill building.

The majority of window displays consist of merchandise and do not feature movement or demonstration. Merchandise should be shown in season. It should have attractive cards giving the price and in many instances facts about the quality or uses should be presented. Merchandise may remind the passers-by that they need the article, or it may remind them that the store has the article for sale. The consumer may be conscious of a need, and the displayed article may provide a new or better way of satisfying it than the article which the customer has bought in the past. Sometimes the consumer will discover a

new use which had not occurred to either the manufacturers or the retailer. The cards giving the names, prices, uses, construction, or other information about the goods may be the decisive factor in drawing the consumer into the store. Many people stop to look at the window and pass on. Others stop and look, start to enter, hesitate, start to leave, look some more, and then some leave and some go into the store. Perhaps it is the price or some descriptive phrase about the goods that draws them into the store. If they do not come in, the salesman does not have the opportunity to show and explain the goods and make the sale.

Arranging Window Displays

Most anyone can wash windows, put merchandise in them, and change the items frequently, but arranging good window displays is an art. The art is learned from experience and study.

Store policy. The windows are the face of the store. They should reflect the store's personality or policies. If the store is a promotional store, the windows should be arranged to reflect this basic policy. The type of window display which an exclusive shop can use to advantage can not be used by the promotional store. The opposite is also true, although some stores which appeal primarily to a higher income group arrange windows to draw a slightly lower income group. The object is to draw the lower income group into the store and "trade them up." Once they make a purchase they may continue to be customers.

Some retailers believe that the same merchandise which is featured in the advertising should also be displayed prominently in the windows. The double emphasis obtained is believed to produce a greater sales volume of the promoted merchandise. In following such a policy it must be carefully determined if the merchandise merits such treatment. If merchandise is slow in selling or has a high markup, it may merit double emphasis. It is frequently not practical, however, to give all the promotional attention to one line of merchandise.

The display theme. Every window display should have a theme or message which the window shopper can understand easily. The theme may be the high style of the merchandise, the low prices of the merchandise, or the variety of merchandise which the store carries. It may be the long number of years which the store has served the community. It may be the January White Sale, or a back-to-school promotion. Whatever the keynote is, no chance should be taken on the customer's failure to interpret it as intended. In case there is any doubt, properly prepared window cards or plaques should emphasize the message.

Selection of goods. Seasonal goods should be displayed in their best selling seasons; those which are sold throughout the year may be displayed at any time. Seasons and customer demands vary, of course, according to the region in which the store is located—Florida and Maine, or Southern California and Minnesota, for example, each have distinctive climates. The following hardware store schedule, however, is typical for any of these localities.

January—Inventory sale: any staple goods, such as tools.

February—Dollar day: any staple goods such as housewares.

March—Lawn and garden tools, garden hose and accessories, seeds, pest controls, ranges (new and used), washers, ironers, housewares, screens, garbage receivers, household and building tools, builders' hardware, roofing, fencing, paint, roller skates, bicycles.

Easter—Grass and flower seeds, bulbs, nursery stock; toys and games for children.

April—Same goods as March. Also sporting goods for baseball, golf, tennis and fishing; automobile goods.

May—Same goods as March and April. Also vacation goods, picnic goods, luggage; gifts for high school and college graduates and June brides; lawn furniture.

June—Gift goods, such as silver sets, glassware, china, electrical appliances, cutlery; vacation goods, picnic goods, insecticides, fans, ice cream freezers, thermos jugs and bottles, fishing tackle.

July and August—Canning supplies, hot weather goods such as fans, freezers, and picnic goods. In late August, school supplies and autumn goods may be shown.

September—School supplies, luggage, bicycles, guns, football equipment; paint, stoves, furnace repairs, stokers, incinerators, gar-

bage cans, tools, electrical goods, builders' hardware, electrical appliances and supplies, weather strips.

October—Most of the goods listed for September. Guns, ammunition, other hunters' goods; woodcutting tools such as saws, axes; chains; rakes, roofing, electric and oil heaters; basketball equipment.

Hallowe'en—Brooms, vacuum cleaners, clothes hampers, irons, cooking utensils, electric heaters, washing machines, rakes.

November—Fireplace goods and fixtures, heaters; snow shovels; snow shoes, skis, sleds, basketball goods, skates; roasters, cooking utensils, Thanksgiving goods, dishes, butchering supplies. During the final weeks, gift goods may be displayed.

December—Gift goods of all kinds, toys of all kinds, skates, sleds, electrical appliances, china, novelties, carpenter's tools, power tools.

December 26-31—Suggestions for spending Christmas money: gifts of all kinds—guns, toys, tools. Any appropriate gift articles which the store has in stock. This may be an opportunity to move leftover Christmas toys and other goods at cut prices to avoid carrying in stock another year.

Displays will vary with the location of the store, the kind of goods carried in stock, and the quantity on hand. As a rule, goods of which the store has a plentiful supply will be used. Related goods usually should be displayed as a unit.

The specific merchandise which is selected for display in the windows should first be carefully inspected and prepared. An actress does not make a public appearance unless she is properly made up. Men's suits with threads hanging from them or with wrinkles in them do not make attractive displays. Frequently the attractiveness of a furniture display is impaired by the use of obviously defective or scratched articles. Furniture and shoes should be polished before being placed in a window. A careful inspection of the merchandise in windows often reveals haphazard selection and preparation of the merchandise.

Background and fixtures. The background materials and fixtures should harmonize with the goods and set them off but should not attract attention to themselves. Unusual or ornate designs and brilliant colors are not suitable unless they are essential to the display—a panorama of a sunset or fire, for example. It is suggested that a set of interchangeable fixtures be

made which can be used in setting up a great variety of displays.

The display fixtures should be inspected periodically and kept in good repair. A soiled or chipped mannequin makes a poor display. Splintered, scratched, or otherwise marred fixtures are likewise unattractive. Ease of maintenance is a factor in the selection of display fixtures: properly maintained fixtures have an influence on the effectiveness of a window display.

The more brilliantly the windows are lighted the more attention they attract. It is often desirable to spotlight certain articles in order to call special attention to them.

An article to be spotted may be placed just inside the door, and, by use of a floodlight, it may be displayed almost as if it were in the show window. This in effect gives the store another window. Of course such an article also gets attention from customers who enter the store.

Price tags. Many retailers believe that all articles in the windows should have price tags displayed prominently with them. Other retailers do not agree with this point of view. A few have made an effort to determine which is best by arranging a window with the price tags prominently displayed and noting the number of people who stopped to view the window and the number of these who entered the store. Later, reactions to the same window with the same or a similar arrangement without price tags or cards were also observed. The results in all reported cases have been in favor of the window with price tags or cards prominently displayed.

Exclusive shops frequently do not use price cards or tags in their windows. The reason is that they are not making a price appeal but are appealing to the customer on the basis of style, distinctiveness of merchandise, and high quality. They reason that their clientele is not interested primarily in price and they do not desire to attract a price-conscious clientele. The number of people who compose this clientele is relatively small.

Color. Color can be very useful in attracting attention and drawing customers into the store. Colors are said to create the following impressions:

Red—Fire, danger, excitability
Yellow—Motion, speed, joy

Blue—Coolness, formality
Green—Rest, peace
Violet and purple—Solemnity, distance, mystery, royalty
Orange—Autumn, sunset
White—Coolness.

Summer displays are usually white, green, or blue. A hot-weather window may use cotton batting as the background to suggest snow for a display of electric fans, a refrigerator, ice cube trays, thermos jugs or bottles, ice cream freezers, and the like. Another summer window might use green on the floor, in the background picture grass and trees, and display a hammock, lawn furniture, thermos jugs, iced-tea glasses or other hot-weather goods. Bright red repulses customers on hot days.

Warm colors—reds, yellows and oranges—are used in fall and winter displays of stoves, heaters, football equipment and other cold-weather goods. White, of course, is used to suggest snow.

Color harmony may be secured by using two hues that are adjacent on the color chart: red and red-orange or red-purple (but not both red-orange and red-purple, as this combination crosses the primary red and introduces three primary hues); or opposite colors on the chart, as, for example, red and green.

Some colors are harmonious (or blend well) and may be used together:

Red with green, cream, silver, gold, brown, or tan
Yellow with violet, purple, or brown
Blue with orange, also with cream, gold, or brown
Green with cream, gold, or red
Orange with purple or blue
Purple with heliotrope or greens
Pink with blue, violet, or heliotrope
Brown with cream, gold, or blues
Gray with blues, pinks, or reds
Maroon with blues or pinks.

Certain color combinations should be avoided by the amateur until he learns to select the exact intensities and values that harmonize:

Red with purple, lavender, pink
Orange with yellow, cream, lavender
Green with yellowish green or light blue

Red-blue with blue
Purple with red
Brown with purple, gray, violet
Maroon with scarlet, purple, violet
Pink with scarlet, red.

Because color aids in legibility it is very important in preparing window cards. The following combinations are arranged in order of their legibility:

Black on yellow background
Black on white
Yellow on black
White on black
Blue on white
White on blue
White on green
Green on white
Red on white
White on red
Red on green
Green on red.

This indicates that most window cards should be yellow or white with black lettering.

Different colors absorb and reflect varying amounts of light. White reflects the highest percentage and black the least. Other colors fall in between; the light colors reflect more light and the darker colors less. Because of this fact, the amount of light used in a window should sometimes be varied according to the colors of the goods on display. If the goods in one end of the window are dark and those in the other end are light, then stronger bulbs should be used in the end with the dark goods. In this situation incandescent lights are better than fluorescent.

Show windows are to set off and display merchandise. The colors used as backgrounds should not divert attention from the goods.

Balance and symmetry. Balance produces an effect pleasing to the eye. The eye very quickly spots things that are "out of balance." The retailer himself can see when he has an unbalanced window if he will look at it from the street.

The easiest way to secure a well-balanced window is to select

the article or group of articles to be featured and place them in the center of the window where they instantly attract the eyes of the passers-by. Smaller articles may be placed in a semi-circle in front of this with balancing displays (larger than the small articles but smaller than the main feature) on the right and left, nearer the front of the window. This arrangement forms a triangle with the window as its base and the central feature of the display as the apex or focal point. This is obvious or formal balance. Hidden or informal balance can be obtained by placing larger articles at greater distances from the central feature so that they appear in balance to the eye. Smaller merchandise of intense color is used to balance the larger-sized but more prosaically colored items.

Lines and shapes. Articles of different sizes should be arranged in natural steps according to size to give perspective to the window. The eye tends to follow lines. Improperly arranged lines may lead the eye away from the displays and not to them. Ribbons or streamers may be used to direct the eye to the goods. Horizontal lines indicate calmness and rest; vertical lines, reliability or strength; diagonal and oblique lines, emphasis or action; gently waving lines are the most attractive but require great care in handling. Circles attract the eye but do not hold attention; they are better, however, than squares and rectangles. Stars, pyramids, and cones are pleasing. The proportion of five to seven to eleven is said to be ideal for solid figures and that of three to five for planes.

How many articles should be placed in a window? The general rule is that a window should not be crowded—that too many different articles should not be shown. In determining how much to put in a window the retailer should consider the purpose of his display. Too many items divide attention. If the object is to introduce a new line or promote the sale of a single item, only that merchandise should be used. A window may contain only one dress, one coat, one washing machine, one refrigerator, or a few silver service sets. The article may be placed in the center of the window, attention focused on it with streamers from the various corners, and a strong spotlight thrown on it. The consumer's attention is concentrated. The

silver sets may be displayed on a piece of velvet or other luxury-type fabric. The one article stands out and the passers-by get an idea that it is important, of high quality, and an excellent value.

There are, on the other hand, reminder-type windows. These are often used by merchandising drug stores. A great many items are displayed with the hope that every passer-by will see at least one item which he needs and will come in and buy it. Hardware stores often use this type of window, especially for their smaller wares. There may be many such small items which the retailer may want to promote from time to time.

Mass displays consist of large quantities of one kind of merchandise. The novelty attracts attention and the quantity displayed sells the idea that the dealer does a big business to have so much of one item in stock.

Clean windows. It seems obvious that the retailer should keep his windows clean. The first thing people see about his store is his windows. If they are not clean, they make a bad impression. They should be kept clean if this means washing them once a week or once a day. They should be kept clean inside as well as out. Care should likewise be taken to keep the floor and sides of the display space clean.

Change. A country crossroads merchant expressed the psychology of changing displays most aptly when he pointed to a child's sweater displayed in his window and said, "See that sweater; it's a nice sweater, all right. But a woman comes in today and sees it. It's new to her and attractive. She comes tomorrow. She has seen the sweater before and it isn't new to her. She comes in the next day. She has seen the sweater twice before and it's beginning to look old. She comes in the next (fourth) day. She has seen the sweater three times before and it looks old to her. She comes in the next day, and the sweater is very old to her because she has already seen it four times. She comes in again (the sixth day) and sees the same sweater and it seems so old to her that she says, 'I never see anything new in this store.' But as a matter of fact that sweater has been on display only one week. This woman doesn't go to the

trading center every day. She goes once or twice a month and what she sees is all new to her and she decides that the stores in the trading center have the newest goods while she thinks I never have anything new. You see why I should change my displays more often than the stores in the city."

Some stores change their window displays weekly, some twice a week, and a few every day. Downtown stores probably change their window displays more frequently than stores in small towns and villages and those in neighborhood business districts of large cities. If the crossroads village merchant is right, however, the village and neighborhood stores should change their window displays more frequently than the downtown city stores.

Windows should be designed so that the displays can be changed easily. Merchandise in shallow open windows can be conveniently reached. Shallow semi-open or closed windows may have hinged or grooved rear panels so that they can be removed quickly for changing the displays or taking out goods requested by customers.

Deep windows may have a walkway along the side wall where the arranger can stand while changing displays or removing goods. Another plan is to mount the entire show window framework on wheels (sometimes tracks are used, too) so that it can be pulled back into the store. After the display is changed it is simply pushed into position. When this plan is followed, floor space must be allowed at the front of the store, which means that platform displays or radiators can not be located directly in back of the window.

Summary of window display policy and practice. Good window display policy and practice may be summarized as follows:

1. The window displays should reflect the basic policies of the store.
2. To obtain a double promotional emphasis, the windows may be used to display the same merchandise which is featured in the advertising.
3. The window displays should have a basic theme or idea.
4. The display should be timely.
5. The merchandise should be carefully inspected and prepared before it is placed on display.

6. The proper background should be used.
7. Fixtures should be inspected carefully before being used in a display.
8. Light should be used properly.
9. Windows with price tags prominently displayed have greater pulling power.
10. Colors of merchandise should harmonize.
11. The display may have either formal or informal balance.
12. The merchandise should be arranged to give the proper perspective.
13. Every window display should have a focal point.
14. The windows should not be overcrowded.
15. Use motion in the display if it is practical.
16. Use sound with the display if it is practical.
17. Display related merchandise.
18. Suggest action by the arrangement of merchandise and fixtures.
19. Show merchandise in use or in customary surroundings.
20. Cards or plaques should present the theme of the window in case there is any doubt about the idea being grasped by shoppers.
21. Art work or other property used with the display should not distract attention from the merchandise.
22. Window displays should be planned and sketched in advance.
23. The glass and floor of the window should be kept clean.
24. The display may be tied to national advertising.
25. Change the display frequently.

Questions

1. What are the three objects of window display?
2. What are some of the devices for attracting attention in window displays?
3. What are spectacle displays?
4. How does store policy affect window displays?
5. Should merchandise which is featured in the advertising also be displayed in the windows?
6. What is meant by a display theme? Illustrate.
7. What points should be given consideration in selecting merchandise for window display?
8. What should be considered in choosing background materials and fixtures for window displays?
9. Should the price tags on the merchandise be displayed prominently in the windows?
10. What is meant by color harmony?

11. How is formal balance attained? Informal balance?
12. What is meant by perspective? How is it attained in window displays?
13. How many articles should be displayed in a window?
14. How often should window displays be changed?

25

Stock Arrangement and Display

THE MANNER in which the merchandise is displayed and arranged aids or hinders its sale. Arrangement of the merchandise in such a manner that its sale is promoted is, of course, most desirable. Either because of inertia or because retailers do not know, merchandise is too frequently poorly displayed and arranged.

Stock Arrangement

There are certain general objectives which may serve as a guide in arranging the stock. For any particular kind of merchandise there are also certain specific objectives or guides. Only the general objectives will be discussed here. The merchandise should be so arranged or located that:

1. The most profitable merchandise is given the best selling location. The front part of the first floor is the most valuable part of the floor space. In a building 100 feet deep, the front 10 feet are estimated to represent about 25 per cent of the value of the entire first floor. The next 20 feet represent 25 per cent of the value; the next 30 feet, 25 per cent, and the rear 40 feet, the remaining 25 per cent. Thus, if a store room 40 x 100 feet rents for $4,000 per year, the average rent is $1 per square foot. The front 10 feet are worth $1,000, or $2.50 per square foot. The next 20 feet have a value of $1,000, or $1.25 per square foot. The next 30 feet have a rental value of $1,000, or 83⅓ cents per square foot, while the rear 40 feet have a rental value

of \$1,000, or 62½ cents per square foot. In a store with two floors, the first floor is usually assigned 65 per cent of the rent and the second floor or the basement 35 per cent. In a store with more floors, the main floor bears a smaller percentage of the total rent.

Because of the high value of the space near the front of the store, the merchandise placed there often has a high volume of sales per square foot or has a high markup. In a department, clothing, or dry goods store, the space near the front is often used for hosiery, men's furnishings, lingerie, jewelry, handbags, gloves, toilet goods, novelties, handkerchiefs, furs, or goods which are being specially promoted. The front space may also be used to build sales for new merchandise or for merchandise which is not selling as it should. Impulse merchandise is often placed near the front so that customers will see it when going to the rear of the store for shopping goods or for staples.

2. The store will have an attractive appearance. In order to secure a pleasing appearance, merchandise which has attractive colors, lines, or finish is often placed near the front and along the main aisles. The merchandise and fixtures are so arranged and selected that easy point-to-point visibility is provided. An unobstructed view is provided over a large space. The stacking of merchandise high on counters and tables is avoided.

3. Customers will be drawn far enough into the store and will see merchandise other than that for which they entered. In order to draw customers deep into the store, shopping goods, articles on sale at especially low prices, or staple necessities may be placed well toward the rear or on upper floors. Because customers expect to devote some time to the selection of shopping goods, they usually do not object to going to the rear of the store or to upper floors for them. On the way they may see other merchandise which they need. Care, however, must be exercised in making this store plan. Convenience goods such as cigarettes, periodicals, toothpaste, razor blades are often wanted by customers who are in a hurry. They prefer not to take the time to go to the back of a store for them.

4. It is convenient for the customer. Merchandise should be

so arranged and located that the customer has adequate room to move around the store. Large people are particularly inconvenienced by narrow aisles. Store traffic is impeded and hazards created by some retailers who place merchandise on the floor along an aisle. Merchandise, to be bought, must be seen. Merchandise placed on a level with the customer's feet is not likely to be seen. If the customer is interested, he must bend over to inspect it—meanwhile he hinders the movement of other customers. Such situations occur in narrow selling rooms where the retailer is attempting to get the most from every square foot of floor space.

5. Related merchandise is located near-by. Articles which are commonly bought or used together should, as a rule, be displayed together. This helps to increase the size of the average sale. Razor blades are placed near shaving soap and these are placed near tooth brushes and tooth paste. Men's hats are located near men's suits. Women's hosiery is located near women's shoes or lingerie. Women's clothing is often displayed near children's clothing, because most of the latter is bought by women.

6. Salespeople can obtain goods quickly and easily, show them properly, and serve customers quickly. A customer may be in a hurry. He does not wish to wait for a salesman to find merchandise which is inconveniently located. Considerable space is needed to show or demonstrate some merchandise. It may be desirable to show much merchandise to the customer, but adequate space must be left for the handling of goods. The tops of display cases should not be entirely covered with merchandise. This not only leaves inadequate space for handling the merchandise but it prevents the customer from seeing what is in the display case.

7. The sale of new merchandise is promoted. New merchandise may be given a preferred location although immediate sales may not justify it. This is done to build sales for the future or to find the sales possibilities of the merchandise. It suggests that the store is up-to-date.

8. Merchandise which is purchased infrequently and about which the customer may deliberate at length is removed from

areas of heavy traffic. By so doing, confusion is avoided and the flow of store traffic is promoted. Men's suits, for example, are placed at the rear of a small store. Rugs, women's coats, and furniture are placed on the upper floors of department stores while candy, notions, gloves, and hosiery are placed on the street floor.

9. The customer is encouraged to serve himself. Wages and salaries constitute the largest item of expense in operating a retail store. When it is practical to arrange merchandise so that the customer can serve himself, it should be done. Fewer salesmen will be required. Work clothing, household hardware, groceries, and many other goods can be so arranged. Prices and sizes must be indicated clearly.

10. It is protected from pilferage. Though it is most desirable to place merchandise where the customer can handle it, this cannot be done when the article is highly susceptible to pilferage. Jewelry and other articles of small bulk and high value are in this category. Consequently, the merchandise must be placed in a show case, under glass, or near the cashier where it can be easily observed.

Display Fixtures

The display fixtures should be suited to the store's clientele. What is suitable for a country general store is not suitable for an exclusive metropolitan apparel shop. The style of the fixtures indicates to the customer whether the store is the kind in which he usually buys. He will feel uncomfortable if the merchandise arrangement and display are not the type to which he is accustomed.

Obviously the fixtures must be suited to the kind of merchandise which is to be displayed. It is not so obvious, however, that one kind will function more efficiently than another. Competing fixtures salesmen will provide information on the merits of their particular lines.

The display fixtures should not be so attractive that they obtain the attention and interest of the customer instead of directing it to the merchandise. High-styled fixtures may do

this. The fixture should not give the impression that it, rather than the merchandise, is being offered for sale.

Display fixtures should be adaptable. This means that counters, cases, drawers and shelving should be of standardized dimensions that are interchangeable. They are thus more adaptable to different display situations.

Although other stores are likely to have the same fixtures, a stereotyped effect can be avoided by the use of the proper decorations.

Easy accessibility is another desirable characteristic of display fixtures. Shelves and drawers should not be too high, too low, or too heavy but should be of the right height and weight so that salespeople can obtain merchandise with ease. Cases that open from more than one side, drawers that move easily on rollers, and bin-top or compartment-type tables should be used.

A commonly used type of display fixture is the aisle table. The merchandise is placed in compartments or arranged on top of the tables. The uses and advantages of these tables are as follows:

1. They can be arranged to direct store traffic to various departments or sections or in a desired direction. By placing the tables in the proper locations store traffic can be directed closer to merchandise which is on display in cases, on cases, or on shelves behind cases. The customer's attention is focused on the merchandise. These tables, however, are frequently located on the main lines of traffic and at peak periods of traffic movement they may hinder the movement of customers.

2. They make merchandise easily accessible to the customer. This is a fundamental of merchandising. The merchandise is presented to the customer's sense of touch as well as his sense of sight. In addition, the customer is encouraged to serve himself. He can select colors, sizes, and the price which he wishes to pay. The salesman needs to perform only the services of wrapping and taking payment. The ready accessibility of the merchandise, however, increases the possibility of shoplifting and causes damage to the merchandise.

3. They create the impression that the store offers merchandise of good quality at a low price. The merchandise featured on the tables is a bargain. Four of the tables may be arranged in "bargain square," and a salesman, with cash register, located inside the square. Stores serving the high-income group, however, may attract the bargain-hunting customer and damage their reputation for exclusiveness.

The beginning retailer with little capital may well make the decision to get along with a minimum investment in display fixtures. The primary consideration is to sell merchandise, and at the beginning of the business what is desirable in fixtures can be sacrificed in favor of a larger stock of merchandise. Much can be done with used fixtures. A new coat of paint or varnish, or a new covering of cloth, linoleum, or other material will make a considerable difference in the appearance of fixtures. In some instances, the retailer can construct his own. His available time, materials, capital, and the inclination to do so are the governing factors. He may prefer to construct some of his smaller fixtures from plans which he draws himself or obtains from published sources.

Lighting

Proper lighting is of fundamental importance to the effective display of merchandise. A given amount of money spent for an increased amount of light will usually increase sales more than an equal amount spent in any other way. Natural lighting is the best but it cannot be controlled even when it is available. There are several advantages of good lighting from the point of view of displaying and promoting the sale of merchandise.

1. Good lighting can bring out the best features of merchandise. It can make colors appear at their best. It can cause shadows or eliminate them.

2. People are attracted to well-lighted merchandise. Light is a basic attraction. It brings attention to whatever may be lighted.

3. Merchandise which is adequately lighted can be inspected more thoroughly by the customer. The salesman can be more effective. Returns are lessened.

4. Merchandise which is displayed in adequate light is kept in better order because the better light brings it more to the attention of salespeople. Orderly displays of merchandise are more appealing to the customer.

5. Good lighting puts the customer in a more receptive mood for suggestions concerning the merchandise. Well-lighted merchandise and surroundings are pleasant and cheerful. The customer is more inclined to be friendly with the salesman.

The lighting in a store is general and local. The general lighting is furnished from wall or ceiling fixtures and local lighting is furnished from fixtures near the merchandise. The light rays may be cast directly upon the merchandise, or into the space to be illuminated, or they may be cast indirectly. With indirect lighting the bottom of the fixture is opaque or otherwise designed to cast the light on the ceiling or walls, from which it reaches the goods or space to be lighted. Indirect lighting gives a better diffusion and prevents glare, but it requires more electricity to provide a given intensity.

The intensity of light is measured in foot-candles, a foot-candle being the amount of light given off by a standard candle at a distance of one foot. For the general lighting of a sales floor the intensity of the light should not be less than 15 foot-candles and as a rule not more than 30 is needed. About 20 may be satisfactory. The intensity of the light is checked with a light meter. The small retailer may have the local electric company check his lighting and make recommendations.

The two types of lamps in general use are the incandescent and the fluorescent. The fluorescent has several advantages: It gives a light similar to daylight (or a colored light) at a high efficiency; it requires less electricity; it gives off less heat; and it has a modern appearance. The incandescent lamp does not flicker, can be used to spotlight merchandise, is easy to maintain, is more flexible and adaptable, and in the past has been more economical to install and replace.

Types of Displays

Interior displays may be classified in several ways: by whether the merchandise is accessible to the customer or whether it is accessible only to the salesman. They may be classified as to the location of the merchandise or as to the characteristics of the merchandise arrangement. They may be classified as to whether they are devised by manufacturers or by the store.

Open display. As previously indicated, it is often desirable to place the merchandise where the customer can both see it and examine it. Variety stores, drug stores, clothing stores, and hardware stores make extensive use of open display. The merchandise is placed on racks, on aisle tables, in bins, or on the tops of counters. Many experiments have been conducted to determine the effectiveness of open display in increasing the sales volume of an item. Normally, substantial increases in sales volume result where merchandise is placed on open display and declines occur when it is not so displayed.

Open displays are easy to change. Partitions, shelves, and doors do not interfere with the placing of merchandise. Gymnastics are not required to place the merchandise where it can be seen easily by the customer. Displays which are difficult to change tend to remain too long unchanged.

Another advantage, which may not be readily apparent, is that open displays create selling space for merchandise which otherwise would be out of sight in the stockroom. Merchandise which is not seen usually sells slowly. Merchandise displayed or stored at the point of sale sells faster.

Open display fixtures are easy to keep clean. Dust does not accumulate in places from which it is difficult to remove. Waxing and polishing of fixtures is done frequently because it is easy to do.

Open display fixtures are usually economical and simply constructed. They are frequently made of wood instead of glass. They have fewer drawers and doors to get out of order.

The selection of merchandise for open display. Certain factors govern the selection of merchandise to be placed on open display. What may be suitable in one store may not be in

another. Obviously the specific line of merchandise which is being sold is a factor.

Slow-selling merchandise may be placed on open display to speed up its sale. By attracting the customer's attention to it more sales are made than when the merchandise is less prominently displayed. This is contrary, however, to the philosophy of playing the winners. Some retailers believe in swimming with the current: they favor merchandise in strong demand for open display.

Specially purchased merchandise may be used for open display. If a large quantity of merchandise has been bought because of an attractive discount, its sale should be pushed or the economy of the quantity discount may be lost because the merchandise remains on hand too long and substantial markdowns are necessary to move it.

Because of the effectiveness of open display, merchandise which the retailer desires to close out may be arranged in this manner. End sizes, unusual colors and styles, or discontinued lines of merchandise will receive more attention from customers and salesmen when placed on open display. By following a regular policy of placing such merchandise on open display, the rate of stock turnover may be improved.

Merchandise with a high margin of profit is often suitable for open display. By increasing the rate of sale a larger stock may be justified. The total gross margin on this merchandise, however, should be compared with the total gross profit on a line that has a smaller markup per item but sells faster.

Novelty merchandise should be placed on open display. There is considerable risk with novelties but it can be reduced if the item is placed on open display. It is likely to sell fast enough so that no loss is incurred if the merchandise suddenly loses its appeal.

Merchandise which is small enough so that all or nearly all of the stock can be held by a single fixture is suited for open display. Men's ties and socks and a variety of hardware goods are examples. If the merchandise has attention-getting colors and finishes, it is very suitable for open display because of its attracting power.

Merchandise which is bought on impulse should be placed on open display. Its sale depends on its being seen. Novelties, food items, magazines, and cigars are in this category.

From time to time it is desirable to experiment with different lines of merchandise. Some of the lines may be merchandise which consumers ordinarily do not expect the store to carry. The sales possibilities of the line can be better determined if it is placed on open display. There was a time when men did not expect to buy shaving supplies in a men's clothing store. Some of these stores, however, put the merchandise on open display in an experimental way and their sales volume justified making the line permanent.

The brand policy of the store may also be a factor in determining what merchandise to place on open display. If the store has its own brand on some lines of merchandise, these items may be given the preferred positions in open display. This procedure aids the store in building its own reputation rather than that of a manufacturer.

Closed display. It is not desirable to place all merchandise on open display. Even in variety, drug, hardware and other stores which make the greatest use of the method, not all merchandise is on open display. Some merchandise is placed on closed display in glass-enclosed cases where it can not be handled by customers.

Merchandise which may be damaged by improper handling should be placed on closed display. Cameras, jewelry, micrometers, china, musical instruments, shirts, expensive garments in delicate colors and other merchandise of relatively high value are examples. Damage caused by excessive or improper handling is expensive. Although a certain amount may be unavoidable, some can be prevented by placing the merchandise in a closed display where the idly curious and unskilled handlers are not able to touch it. The merchandise can be obtained easily for customers who express an interest in it.

More expensive merchandise should be placed on closed display because of the theft hazard. The higher the price of the merchandise, the greater the temptation to theft. If the merchandise is also small—jewelry, for example—then the hazard

of theft is further increased. Even relatively large items such as fur coats, musical instruments, and silverware may be purloined if placed on open display.

Merchandise which sells faster when displayed with related merchandise should be placed on closed display. When related merchandise is placed on open display it does not long remain in the proper relationship. Handling by customers soon destroys the effectiveness of the display.

The very fact that merchandise is placed on closed display increases its appeal to some customers. This may be because of the merchandising custom over a long period of time of showing expensive merchandise inside glass. The customer has come to associate high value with merchandise displayed inside glass cases. When the merchandise is arranged carefully it is attractive and remains that way while on display. Consequently, it attracts favorable attention. For this reason, slow-selling merchandise may have its rate of sale increased by placing it in a closed display.

Closed display appeals to those customers in the apparel market who desire exclusiveness. Consequently, stores which make that appeal use open display very sparingly because their clientele desires merchandise which has been protected from handling. Exclusive stores use more closed display and also keep much of the merchandise out of sight in drawers and special sections.

The Arrangement of Merchandise in Displays

Merchandise should be so arranged in displays that the customer's attention is attracted, his interest aroused, his desire stimulated, and the completion of the sale made easy. Attention can be attracted to a display by placing it where it is most likely to be seen—where the customer's eye tends to focus temporarily. A study of customers as they enter and move around the store will indicate the spots which most frequently receive attention. An analysis of the reason why these places receive attention will reveal their display possibilities.

In a large store equipped with escalators, the attention of

customers traveling by this method is to the open side of the escalator. In some stores attractive displays are located at a point where the customer can observe the merchandise as the escalator moves along. In other stores, however, no such displays are arranged; the customer's attention wanders over an entire floor and is not directed to any particular merchandise. This would seem to be a wasted opportunity.

As the customer rides down an escalator his attention is usually focused on the foot of the section he is riding. This terminal spot is also a place where a display should be located. As customers ride an up-section their attention will be drawn to a display at the head of the section if one is located there.

In many small stores there are two blind spots to the customer who is entering, one to the right and one to the left of the entrance. The departing customer sees these locations, but often no merchandise is displayed in them. Frequently the ends of counters or cases and doors to the windows cut off his attention. There may be merchandise in the cases near the door, but the cases are arranged parallel to the customer's progress and below his range of attention. Consideration should be given to a different arrangement of the cases. In narrow rooms perhaps no change can be made, but at least an attractive top-of-the-counter display can be arranged. Clothing retailers use the color appeal of ties, socks, and sweaters advantageously at these spots.

It would be impractical, of course, to arrange merchandise displays at every suggested possible point in the store. To do so would scatter the attention of the customer instead of concentrating it. Some retailers have accepted manufacturer-built displays without discrimination, which, when added to those devised in the store, give it a cluttered appearance. Some displays, placed high above the range of the customers' attention, gather dust because of the difficulty of changing them.

Customer attention must be held if interest is to be aroused. The giving of undivided attention is difficult. It will be, or perhaps can be, achieved only for brief periods. Every advantage, then, must be taken of conditions in the area to facilitate gaining undivided attention. The retailer or display manager

must therefore be constantly on the alert for devices which will attract and hold attention.

A sale will not follow if the customer's desire is not stimulated to the point where he is ready to make a purchase. Desire can be stimulated by the manner in which the merchandise is arranged. It can also be stimulated by the copy on a card which appears with the merchandise.

The sale can not be completed, however, by the display. The services of a salesman are required even though nothing more than wrapping and accepting payment are needed. The completion of the sale can be facilitated if an alert salesman is stationed near an effective display. The right word at the right time will make a sale when otherwise the customer might turn away.

Every display should be analyzed from the point of view of its ability to attract attention, arouse interest, and stimulate desire. Frequently, other sales promotion media have carried the customer part way along the route of a completed sale. An effective display will bring him farther along, or perhaps prevent him from turning back.

Questions

1. What are the general objectives which may serve as a guide in arranging stock?
2. What merchandise should be placed in the front part of a small store? In the rear?
3. Where should the retailer place merchandise about which the customer deliberates considerably before making a purchase?
4. What standards should display fixtures meet?
5. What are the advantages of aisle tables?
6. What are the advantages of good lighting from a display point of view?
7. What is general lighting? Local lighting?
8. What is an open display? What are its advantages?
9. What governs the selection of merchandise for open display?
10. What is a closed display?
11. What merchandise should be placed on closed display?
12. What should every interior display attempt to do?
13. When should convenience goods be placed in the rear of the store and when should they be placed near the entrance?

14. A store advertises a special sale of hosiery. Under what conditions should the hosiery be placed near the entrance, and under what conditions should it be placed in the rear of the store or on an upper floor?
15. A store selling women's shoes has no shoes in sight except a few pairs in display cabinets and in the show windows. When a customer comes in, she is seated and her foot is measured. The salesman then goes behind a partition and brings out a pair of shoes. If this pair is satisfactory, no other shoes are shown the customer.
    (*a*) Is this a good method of displaying and selling shoes? Why or why not?
    (*b*) If you feel that this method has some merit, to what types of goods or to what types of customers is it applicable?
16. How is customer frontage increased by well-designed layout?
17. Brown Bros. have a one-floor-and-basement store handling the following lines of goods: women's hosiery; women's gloves; women's underwear; furs; handkerchiefs; towels; women's coats; dresses; notions; handbags and novelties; men's furnishings; men's suits and overcoats; work clothing, including overalls, shirts, pants, socks, and shoes; house dresses; women's shoes; men's dress shoes; blankets and bedding; luggage; and kitchen supplies, such as cooking utensils, cutlery, and woodenware.
    (*a*) Which lines should be placed in the basement and which on the street floor?
    (*b*) The street floor is wide enough for a main aisle and two side aisles, all three aisles running lengthwise of the store. Draw a diagram showing the proper arrangement of the lines which you would place on the street floor.

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The Essence of Salesmanship

CUSTOMER, merchandise, and salesman are involved in the selling process. First consideration must go to the customer, but almost as important is a knowledge of the merchandise. How the salesman should present the merchandise to the customer is the essence of the selling process.

The Customer

It is important that the salesman understand the behavior of the different types of customers. Information which will aid the salesman in handling the customer is often obtained during the sizing-up process and as the sale progresses. As the customer approaches the salesman and his department, or as the salesman approaches the customer, he studies or sizes up the customer. This observation continues as long as the salesman has contact with the customer. The purpose is to determine the best manner in which to begin and complete the sale.

Types of customers. Customers have been classified according to the personality traits which they exhibit during the selling process. They may be classified as follows: The decided customer; the know-it-all customer; the suspicious customer; the impatient customer; the deliberate customer; the tired and nervous customer; the talkative customer; the silent and timid customer; the hurried customer; the decided-but-mistaken customer; and the I-get-a-discount customer.

The decided customer knows what he wants and the salesman

should get it quickly. In answering questions and giving information about the product, the salesman should give specific facts and should not waste time in generalities. The salesman may sell additional merchandise if the customer is not in too great a hurry.

The know-it-all customer gives the salesman little credit for knowing his merchandise and wants to tell him "what's-what." If he has the time, the salesman may listen and let the buyer talk himself out. Even if the customer makes incorrect statements, the salesman should not contradict him. He may give the correct information in a tactful and perhaps a roundabout way. He should not appear to notice the mistake and his correction should not be so obvious as to embarrass the prospect. If the salesman in this way demonstrates that he really knows his merchandise, the know-it-all customer may change his attitude. Even if the customer is a boastful bluffer, it is usually poor salesmanship to argue with him.

The deliberate customer takes his time to consider every purchase. He wants facts, and sometimes advice, as to the construction and use of the product. The salesman may excuse himself temporarily to wait on another customer.

The undecided customer doesn't know what size is needed, what color of suit he wants, or what height step-ladder would be best. The salesman should try to determine what this customer needs, direct his attention to it, and help him make up his mind. After showing several articles he should take away those that interest the customer least. The customer's attention is then narrowed and his decision becomes easier. The salesman may unobtrusively take away the goods until the customer has only one or two articles to consider. In other words, the salesman helps this customer make up his mind and, if he sells him what he needs, may win goodwill for himself and the store.

The talkative customer wants to talk about any and everything except his purchase. If there are no customers waiting, the salesman may enjoy visiting with him for a few minutes. The problem is to direct the customer's attention to his purchase. The salesman should not ask questions that will keep

the man talking unless he has time to listen. Once the purchase is made, he should wrap it, make change quickly, and be ready for the next customer when he appears.

The silent, timid customer may feel out of place in the store and fears that he will show his lack of knowledge by asking questions. As soon as the salesman determines what the customer wants, he should give information about the product in a manner which suggests that few people know these things. The salesman should never in any way belittle the customer's lack of information. He should make the customer feel at home in the store and to do so may volunteer information about some of the other merchandise on display.

The decided-but-mistaken customer comes to the store for a definite article but the salesman realizes that the article is unsuitable for that use. For example, the customer asks for flat paint but the salesman finds that the customer wants to put enamel over it and should use a primary coat first. In this case, the salesman should not argue or dispute but should tell the customer the advantage of the undercoating and suggest its purchase.

The "I-get-a-discount" customer wants a discount or cut price. If the store operates on a one-price policy, the salesman must refuse. If one customer secures a discount, he may tell his friends and the latter will soon ask for a discount, also. The store may follow the policy of giving discounts to special classes of customers. If this is the case, the salesman must determine if the customer is entitled to a discount and, if so, the size of the discount. Some people will ask for discounts when they are not entitled to them.

Buying motives. Irrespective of the type which a customer may be, he is influenced by certain "buying motives" or appeals. Some customers respond more quickly to certain appeals than they do to others. It is possible to make a long list of appeals, but a great deal of merchandise can be sold by making an appeal to the customers' desire to be economical, to their pride, to their desire for convenient things, and to their desire for health.

Pride is one of the most fundamental of the buying motives.

The customer who is stimulated by this appeal desires to be distinctive, to stand out from the crowd, to be a leader. He buys merchandise because it is the latest fashion or is up-to-date. He is interested in the lines, finish, and color of the merchandise. This is an emotional appeal. It is not made to the customer's reason.

Economy or the desire for gain is also a strong buying motive. With the saving from an economical purchase the customer can have more goods or services. This desire is so strong that some customers will buy the lowest quality of merchandise in the belief that it is always the most economical. If the salesman suggests an article of higher quality, these customers may feel that the salesman is trying to deceive them by selling them the same quality at a higher price. Economy appeals to the customer's reason rather than to his emotions.

Convenience is an appeal which can be made by pointing out how the merchandise will save the customer's effort and time. It is highly effective in selling labor-saving devices. Household equipment of various kinds reduces the amount of effort and time necessary to accomplish household tasks. Proper tools save effort and time for the artisan or craftsman. This appeal can be made effectively on a logical basis.

The desire for health is one which may not be readily apparent but it is fundamental. The person with a strong body and mind has had a certain advantage since the days of savagery. Perhaps subconscious realization of this fact makes this appeal effective. If the merchandise will protect the customer's health, this fact can be pointed out. Health-conscious individuals or those with ailing bodies are usually more susceptible to this appeal than are others.

Knowledge of Merchandise

Most stores sell so many articles, some of them more or less technical in nature, that it requires a long time and much study to learn the facts about their construction and use. However, this does not excuse an experience like the following: A customer visited a hardware store and asked to see a hammer. A

salesman handed him one and said, "That's a mighty fine hammer. That's a real hammer. We sell a lot of these." The customer looked at the hammer and felt of it. After a time the salesman said, "That's a mighty fine hammer. That's a real hammer. You can't go wrong on that hammer." The customer continued to hesitate, and after a time the salesman said, "That's a mighty fine hammer. That's a real hammer. You can't go wrong on that hammer." The customer didn't buy the hammer. He left the store and later looked in a mail-order catalog. One of the captions read, "This hammer is full nickel-plated. The handle is mahogany-finished and made of selected second-growth hickory. The head is made of crucible cast steel. The claws are tempered just right and are split to a fine point." The hammer shown in the hardware store had all of these features and more but the salesman who showed the hammer to this would-be customer did not mention them. Perhaps the salesman thought the prospective customer could see that the hammer was nickel-plated and had a mahogany-finished handle. Most of us, however, see only the things we are shown or which we are trained to look for.*

If a salesman knows hammers, he knows the relative advantages of round and hexagonal heads, why the head is hard on the surface and soft inside, why the claws have a different temper from the head, and why the handle is unpainted. He does not need to tell every customer all these facts. He may not mention any of them with many customers; but he needs the facts for the customer who wants them and who needs to be sold on the quality of the product.

Reasons for having a thorough knowledge of the merchandise. A number of reasons can be given why the salesman with a thorough knowledge of the merchandise will sell more merchandise.

1. He has more confidence in himself. A salesman attempting to sell some product about which he has little knowledge is unsure of himself and his uncertainty distracts him. Fortified

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* Adapted from "The Hammer Story," pages 203-208 of Paul W. Ivey, *Successful Salesmanship*, 2nd ed., New York: Prentice-Hall, Inc., 1947. Copyright, 1937, 1947, by Paul W. Ivey.

with knowledge, a salesman has a confidence in his selling ability which he will not have otherwise. He can speak with authority about the goods.

2. Customers easily recognize the salesman who knows his goods. The confidence with which he speaks about the merchandise causes them to have confidence in the salesman.

3. A salesman with a thorough knowledge of his merchandise will be more enthusiastic about it. No one can get enthusiastic about something of which he has no knowledge. For instance, a salesman cannot become enthusiastic about period furniture if he does not know it thoroughly enough to appreciate its value. Enthusiasm is catching. If the salesman knows his merchandise thoroughly, his resulting enthusiasm will be expressed and transferred to the customer.

4. The more knowledge a salesman has about his merchandise, the more selling points he will be able to present. Every salesman knows that different customers are influenced by different selling points and that by having a large array to select from, his percentage of sales will be increased. Selling points which appeal to a given type of customer can be selected and presented.

5. "People don't see what they look at." When the customer looks at the merchandise, he may not see or understand its advantages and usefulness. In many cases the customer will never see the advantages of the merchandise if the salesman does not know them himself. Many customers would not recognize that the piece of furniture was solid walnut and of rare design unless such facts were known and appreciated by the salesman.

6. The salesman who knows his merchandise can give customers better service. For instance, the salesman may tell the customers a lounging robe will not shrink if laundered in a certain way, or that better results will be obtained in repainting kitchen furniture if all old paint is removed first. Such action gains the customers' goodwill, prevents complaints from arising, and leads to more sales. The salesman who does not have an adequate knowledge of his product, however, is unable to give customers the proper service and in the long run does not make as many sales.

7. If a salesman knows his merchandise thoroughly, he is able to point out its advantages over competing merchandise. The customer may continue to believe a competing article is better unless the salesman is thoroughly acquainted with the superiorities of the merchandise he is selling and discusses them.

8. The salesman can more effectively meet objections and answer questions concerning the merchandise. He not only has the right information but he can provide it quickly. A salesman who hesitates in answering a customer's searching question tends to lose the customer's confidence.

9. Sales can be made in less time when the salesman has a thorough knowledge of his goods. The informed salesman knows what to say about the merchandise and how to say it. No time is lost in searching for information.

What to know about the merchandise. When the beginning salesman asks the older salesman what he should know about the merchandise, the temptation is to answer "everything!" This is probably impossible, but after several years of experience a vast amount of knowledge is accumulated by the alert salesman.

The amount of knowledge needed depends on several circumstances. Where a wide variety of products are handled by a store or department, it is undoubtedly better to know a little about each item rather than much about a few items and almost nothing about the remainder. More should be known about the most profitable articles than about the items yielding little or no profit. The expensiveness of the merchandise also governs the amount of knowledge the salesman should possess. For instance, the fur salesman must acquire more information about his merchandise than must a salesman in handkerchiefs although a great deal of knowledge can be acquired concerning handkerchiefs. Necessities such as food require less sales knowledge than do luxuries such as oriental rugs. More knowledge is needed about a complex product, for instance a typewriter, than is needed about a simple ruler.

Location of stock. One thing which will give a store a reputation for good service is the ability of the salespeople to locate and produce the merchandise quickly. It is not difficult to

arrange the goods in some kind of system; with a little observation the system in any store or department can be recognized. If the salesman cannot locate the stock quickly, time is wasted and the customer may be irritated by the delay. By locating the stock quickly the salesman often succeeds in obtaining the customer's confidence.

Not only should the salesman know the location of the merchandise requested, but he should also be able to suggest and locate substitute merchandise when the item asked for is out of stock. Likewise the advertised merchandise should be located readily.

Care of stock. Poorly kept stock gives a poor impression of the store. The salesman must know the proper methods of taking care of his merchandise. Shopworn goods lose profits for the store, which in the long run means that the salesman's salary can not be as high as when merchandise is properly cared for. Stock must be kept orderly and in its proper place—tables, hangers, shelves, drawers and so on. It must not be left scattered haphazardly on counters or across chairs. Although it is a virtue to return the stock to its proper place, this work must not be done if customers wanting attention are present. Stock must also be dusted frequently, surfaces should be polished, and broken, torn, or missing parts replaced.

Correct names. Difficulties with the correct names of articles and parts seldom arise. It is easy, however, to slip into the habit of using slang or technical terms rather than the preferred terms. An article or part of articles should not be referred to as a "gadget," a "doodad," or a "jigger" when gauge, clamp, or connector are the correct terms.

Name and location of manufacturers. If the name and location of the manufacturer are not given on the article itself, the salesman should consult the store buyer or one of the standard directories of manufacturers such as *Thomas' Directory of Manufacturers,* or *McRae's Bluebook.* The manufacturers of a given city or district may be known to produce high-quality products, and their reputation may be a decided help in selling the product.

Sizes and colors. When there are a variety of sizes and colors

available in a given line of merchandise, salesmen should know which items are regularly obtainable from stock and which can be secured only by special order. Where sizes are marked in a combination of numerals and letters, the salesman must learn the size system. Color is a matter of emotional appeal. It can create a favorable or a poor impression. The salesman should know how to display the merchandise so that the colors used will make a strong appeal. This may require arranging a combination of articles. Some dyes are not as fast as others. The salesman should know whether the merchandise is fast color or likely to fade.

Fashion. The salesman must know which styles are becoming popular and which are going out of fashion. He should understand what makes fashion and he should know what is suitable for certain times and customers. Fashion is important in a wide variety of articles from picture frames to chinaware. The salesman should be acquainted with the fashion cycle in his line of merchandise.

Prices. In most cases the salesman will have no difficulty in determining the prices of the merchandise he sells; usually the price will be marked clearly on tags, boxes, or the article itself. The chief thing the salesman may have to learn is what prices to put on the articles when marking them for sale. Prices, however, often vary for quantities, for complete sets (chinaware or silverware, for example) or for a complete assembly like an automobile muffler and exhaust assembly. The salesman should know the trend in the prices of the merchandise he is selling. Most customers will appreciate a suggestion to buy now if the salesman knows that the next lot of merchandise is to be marked higher. Likewise, the salesman must be prepared to push those articles with declining prices since the store may suffer a loss if these articles are not sold quickly.

Quality. The salesman should be able to recognize quality in the merchandise he sells. He should know what makes the superior quality of a given article and why a certain article is of the lowest quality. In general, customers are poor judges of quality particularly in the case of textiles. They often depend on feeling the material although even the best judges of

fabric sometimes make mistakes when relying on "feel" alone. A higher price often denotes a higher quality which the customer may fail to appreciate unless the salesman explains it.

Proper use and care of the merchandise. Knowledge of the proper use and care of merchandise is the most important. If the salesman knows the correct manner in which the merchandise should be used, how it should be cared for, and so informs the customers, many friends will be made for the store and misunderstanding will be prevented. Customers often return merchandise with the charge that it is unsatisfactory. Upon questioning it is often found that the customer has used the merchandise improperly. A customer may attempt to operate an electrical appliance on direct current when it is designed specifically for alternating current only. The fact that printed instructions were enclosed with the appliance may partially excuse the salesman but it will not satisfy the customer. Whenever practical the customer should be given oral and printed instructions. Articles of clothing must be cleaned or laundered correctly. Machines must be oiled, tires must be properly inflated, and paint and varnish must be applied correctly.

People do not buy a product primarily because it is manufactured by a certain company, or because it is produced under certain conditions from certain raw materials, or because it operates this or that way, but they buy the product primarily for what it will do for them. A retailer does not buy a cash register because it has so many keys or because it operates in a certain manner; he buys because it improves his store system. A purchaser of a filing system does not buy so many folders and drawers of a certain size, but he buys smoother office operations. An owner of an automobile does not purchase a tire because it is composed of a certain number of plies; he buys because it gives him mileage and comfort. The product may contain raw materials and workmanship which make it the highest quality, but unless the prospect is made to see what high quality means to him, he is not likely to buy. A detailed description of the product's merits is likely to avail little if the prospect is not shown clearly how the product will help *him,* what it will do for *him.*

Guarantee. The salesman must know what merchandise is guaranteed and the nature of the guarantee. If goods are guaranteed the salesman has a strong selling argument, but the nature of the guarantee must be made clear to customers in order to avoid misunderstandings and dissatisfaction in case claims are made for repairs, replacements, or refunds not covered by the guarantee. Most guarantees agree to replace articles or parts which prove to be defective in workmanship or material. They do not agree to make replacements in case the customer does not follow the instructions for the proper care of the article. Merchandise damaged as the result of improper use or carelessness is not ordinarily covered by the guarantee. For instance, ice skates could not be guaranteed to hold an edge if used on icy pavements. Some guarantees are for the life of the article and some are for a year or a limited time. The customer must be informed of the length of the guarantee period to avoid disagreements over claims made after the guarantee expires. It should not be taken for granted that the guarantee will be read and understood by the customer. The salesman should read and explain it to him.

Selling Techniques

During the selling process the salesman applies his knowledge of customers and merchandise. Some of the techniques of selling will be discussed in this section.

The approach. The approach is the way the salesman comes toward and greets the customer. Much has been said about the proper greeting, but when it is all summed up it seems that what is said is far less important than how it is said. The tone of the voice and the facial expression are important. In fact, a good salesman may not say anything but come to the customer and by his manner show he is at the customer's service. Recommended greetings are: "May I help you?" or "Good morning, may I help you?" If the salesman's tone is right, the following are also satisfactory: "What may I show you?" or "May I show you something?"

The approach should vary with the customer. Well-known

customers are greeted in one manner while others are greeted differently. One who comes in with a definite need in mind wants to be served quickly. The salesman can often spot such a customer by his walk. If he comes in rapidly and walks to a definite place in the store, he very likely knows what he wants and will appreciate prompt service. On the other hand, the customer who comes in "just to look around" should not be hurried. Such a customer should not be met at the door and immediately asked: "What do you want?" or "What can I get for you?" The proper approach for such a customer is to let him pretty much alone although he should, of course, be made welcome. If the salesman has no other customers he can wait at a respectful distance to be on hand if the customer wants some information or advice, or makes up his mind what he wants. Between the customer with a definite need (the destination buyer) and the customer who is just looking around are many customers who do not know exactly what they want.

It is usually wise not to begin the sale with a series of questions concerning price, size, style, color and other features which the customer has in mind. By so doing the customer may be committed to something which is not in stock. Furthermore, the salesman gives the impression that he does not know how to sell and he may make the customer feel ill at ease.

The determination of the customer's needs. Most people who enter a store do so to satisfy a definite need but many of them do not know exactly what they want. A woman may want a saucepan but not know the exact size she wants nor whether she wants cheap enamel, good enamel, or aluminum. A man may want some paint but not know exactly the kind or shade.

The salesman should find the use to which the merchandise is to be put. The way paint is to be used determines the kind needed; outside paint and inside paint differ. Is it a new job or a repaint job? Is the paint to be on wood, plaster, concrete, or brick? Is it an inside wall that should reflect the light, as in a school room? A good paint salesman must know his product if the customer is to be served well.

When the salesman knows the merchandise and how it is to be used, he is in a position to help the customer select the proper

goods. Perhaps the customer had in mind a heavier or lighter quality or grade than is needed. One of the large rubber companies found by consumer research that its lowest-quality hose satisfied the consumer, lasted as long or longer than expected, and was lighter to move around the lawn or garden than a heavier hose. This company had been encouraging its dealers to "trade up" consumers to a more expensive and heavier hose. The company changed the advice which it gave its dealers and offered a quality to meet chain store prices.

If a consumer comes to the store expecting to pay a high price and the salesman shows him that he needs, and can economically use, a lower-priced product, the consumer will have a friendly feeling for the store and will be likely to come back for other purchases. Goodwill is created in this way. There are, of course, many instances when the salesman should recommend a better-quality and higher-priced article than the consumer has in mind. If the store has previously shown the customer how to save money by buying a different article, or a lower-priced article, he will very likely follow the salesman's recommendation and buy the more expensive article and again be better satisfied.

One method of determining the customer's needs is to show merchandise and to note the customer's reactions. By facial expression, comment, or question he will indicate his thought concerning the merchandise. Proper questions will bring out additional information. Sometimes the salesman may be uncertain as to what quality of merchandise to show. In such a case a medium quality of merchandise may be shown. It is usually desirable to place the merchandise in the hands of the customer. This may be delayed until certain features of the merchandise have been presented. Where practical, the merchandise should be shown as it will appear in use. A necktie is held and wrapped as if tied, household furnishings are often displayed as they would appear in a home, and apparel is tried on.

Meeting objections. The first principle in meeting objections is to avoid an argument with the customer. It is not an opportunity for the salesman to prove how little the customer

knows. It is an opportunity to create in the customer's mind a favorable opinion of the merchandise being discussed. The customer can not be forced or argued into this position. It is too easy for the customer to walk away from the salesman.

The salesman should determine whether the objection raised by the customer is merely an excuse or a real objection. The customer will make excuses for not buying when his desire for the product has not been aroused sufficiently. Excuses should be ignored and the sale continued. Real objections should be answered immediately and decisively.

The customer, for example, may refer to the advantages of a competing product. When such an objection is raised, the salesman should not deny the advantage but should point out the advantages of his own merchandise. The customer may be mistaken in his idea of the competing product's advantages. If he is misinformed, he will dislike being told brusquely that he is wrong. It is not necessary to disagree bluntly with the customer. The salesman may give the impression of agreeing with the customer by saying, "That's what I used to think, but . . ." He then proceeds tactfully to point out why the customer's objection is not valid. Or, the salesman may begin, "It appears that way, but . . ." The salesman thus does not directly deny the validity of the customer's objection but indirectly he does. The customer is let down easily. His ego is not injured. This is known as the indirect denial method of meeting objections.

Since most objections are raised often enough to be classified or typed, standardized answers should be prepared for them. This should be done whether the salesman is experienced or inexperienced. If an experienced salesman will write out what he actually says in answer to a given objection, he may discover how poor are some of his answers.

Probably the most common objection is "The price is too high," and probably the most common method of answering it is to point out the superior quality of the merchandise. The higher price is offset by the higher quality of the merchandise. This objection may be answered by showing the durability of the article. That is, by dividing the number of years, months, weeks, or days of the life of the merchandise into its price and

getting a price per unit of time. This frequently closes the sale.

The substitute sale. The customer may call for a specific article or brand of merchandise which is not in stock. At such times the unskilled salesman is likely to make such statements as "We don't carry that any more," or "That's out of style," or "We don't have any calls for that any more." During World War II when the standard of retail salesmanship reached a new low, the customer was answered with "Don't you know there's a war on?"

The proper method of attempting to sell a substitute article is to produce the substitute promptly and explain that it is very similar to the one requested. Then, explain its points of superiority over the requested article. Frequently, the customer will become a steady purchaser of the substituted article.

The article or brand of article requested by the customer may be in stock but for various reasons it may be desired to sell a slightly different article or another brand. The store may prefer to sell its private brand rather than a national brand, or one of two similarly priced articles may yield a larger profit. Whatever the reason for making the substitution, the requested article should be produced promptly and the salesman should show a willingness to sell it. The substitute can then be produced and its points of superiority explained.

If the customer apparently is in a hurry, a substitution should not be attempted; nor should a substitution be attempted if the customer appears to be unreceptive to suggestions. When the substitute is presented its points of superiority should be specifically stated. Some salesmen have nothing more to say than "This is just as good." The customer may doubt or may be puzzled by this statement.

The close. When merchandise has been properly presented by the salesman, there is likely to be very little difficulty in bringing the sale to a close. The customer who is unable to reach a decision may be helped by being asked which of two colors, two styles, or two of any other product characteristics he prefers. By answering the question the customer makes a decision. The customer may be asked if he wishes to charge the article or pay cash. He may be asked if he wishes to take it with

him or if he wishes to have it delivered. Whichever choice is made, the sale is closed.

A frequently used method of closing is known as the S.R.O. (standing room only) method. However, customers often resent this technique. It is based on the customer's disposition to avail himself of an opportunity before it slips away. The salesman suggests that the price may be higher next week, that the store is not likely to receive any more of the merchandise, that the item is the last one in stock, or that the article may not be here tomorrow. Because many customers doubt the truth of such statements, general use of the method should be avoided.

Some customers who obviously have decided to buy cannot come to the point of expressing this decision. Frequently they may be waiting only for the salesman to take the initiative and close the sale. The salesman, recognizing the situation, should start filling in the sales slip, or wrapping the article, or making other motions which assume the close.

A direct question is also used to close sales. The salesman asks such a question as, "Shall I send it out to your house?" or "Do you wish to pay cash?" If a close is not obtained, the salesman may present additional selling points.

All attempted sales are not closed, and it is advisable not to expect to make a sale to every customer who enters the store. To attempt to make a sale to every customer who enters the store will build a reputation for "high pressure selling." Such a reputation hurts future sales.

Suggesting an increase in the purchase. Many possible sales are lost because salesmen do not suggest the purchase of additional articles. A larger quantity of the merchandise may be suggested, particularly when the article is multiple-priced—that is, three, six, twelve or other quantities are offered at a reduction from the price of a single-unit sale. Related merchandise may be suggested. When a shirt is purchased, a tie may be suggested. When shoes are purchased, hose may be suggested. Unrelated merchandise may also be suggested. The unrelated merchandise may be new, seasonal, or specially advertised goods.

The salesman's remarks in suggesting additional merchandise should be specific and positive. Such statements as the follow-

ing are made too often: Something else? Did you wish something else? Was there anything else? What else can you think of? Is there anything else you can think of? Is that all? Nothing else, was there? These questions are poor; they are general, negative, and neutral. Good salesmen very seldom ask them.

Questions

1. Give a classification of retail customers. How should each type be handled?
2. Select some article and indicate how it can be sold by appealing to the buying motives of pride, economy, convenience, and the desire for health.
3. Why must a salesman have a thorough knowledge of his merchandise?
4. What should the salesman know about the merchandise he sells?
5. Why should the salesman be thoroughly familiar with the use of an article? With the guarantee?
6. Should a sale be opened with a series of questions? Discuss.
7. How is a customer's need determined?
8. What is the first principle in meeting objections?
9. How should the customer be handled who asks for an article that is not in stock but for which a satisfactory substitute is available?
10. How may the salesman help the undecided customer to reach a decision?
11. How may the size of the average sale be increased by the salesman?
12. To what extent is the employer responsible for teaching the salesman what he needs to know about the goods? To what extent is the salesman responsible for securing this information for himself?
13. Some stores teach their salespeople to substitute goods under their own private brands or other goods carrying larger margins on every possible occasion when goods carrying smaller margins are requested. Other stores instruct their salesmen never to substitute. What do you think of these two policies? Which is the better? What policy should a retailer follow in regard to substituting?
14. Visit retail stores and rate the salespeople who wait on you. Use the form on the next page. You do not have to make purchases, but you should act naturally as a real prospective buyer. (Prepare the necessary blanks for the number of reports required by your instructor.)

SHOPPER'S REPORT ON RETAIL SALESPEOPLE

Store..

Date and hour..

Name or number or description of salesperson...................

....

Article..

Points observed:	Value	Rating: Good	Fair	Poor	Remarks
Appearance	15%				
Approach	10%				
Interest in customer, merchandise, and store	15%				
Knowledge of goods, uses, colors, qualities, style, etc.	25%				
Force or ability to create desire	35%				
Total rating percentage	100%				

(80–100%, Good; 60–79%, Fair; under 60%, Poor)

Comments:

Did salesperson offer to substitute?
Did salesperson use suggestive selling?
Promptness in wrapping, making change, or making out sales slip or want slip?
Did salesperson call back amount of money in making change?
Would you want the salesperson to wait on you again?
Other comments:

15. A customer brings back a tennis racket saying that there is a defect in its strings because they broke in the first set that was played. An examination of the strings shows that they are pretty badly worn and without a doubt have been used for much more than one set. The guarantee of the racket is against

any defect in workmanship or material; it does not appear that the strings have broken on that account. The man is a good customer and it would be disadvantageous to lose him.

How should the salesman refuse the request?

16. A customer of a furniture store asks for the price on a particular bedroom suite and the salesman gives it to her. She likes the suite and says that she will pay cash for it if the store will allow her $25.00 for her old bedroom suite. It is the policy of the store not to permit old furniture to be traded in on new furniture. Its prices are set on a cash basis and a carrying charge is added for time payment, but provision is made for trade-in furniture. The store, however, will take the old furniture and sell it for the best price that it can get and apply the proceeds on new furniture. The only other real competitor of this store in the town has a very liberal trade-in policy.

    Can the salesman keep this sale from going to the other store? If so, how should he proceed?

E. Finance and Control

27

The Extension of Credit

EITHER consciously or unconsciously a retailer makes a number of policy decisions when he adopts a credit policy. He decides whether he will sell only for cash or whether he will extend credit. If he sells on credit, he must decide whether he will grant limited amounts and for limited periods to only the best risks, or whether he will grant liberal credit to almost anyone who asks for it. He must decide whether he will advertise his credit service. He must also decide the type of collection policy to follow, whether it will be aggressive, moderate, or easy.

The merchandise sold influences the credit policy. If the retailer sells farm implements, dairy equipment, large electrical or gas appliances, furnaces, plumbing equipment, stokers, furniture, or stoves he will probably make a part of his sales on the installment plan or on long-term credit. Since the notes are often sold to finance companies or banks, many retailers consider installment sales as cash sales.

Selecting a Policy

Selling for cash only. There are advantages in operating on a cash basis. Because it does not tie up capital in accounts receivable, it permits the retailer to carry a wider selection of goods. It reduces expenses since there is no need for customers' ledgers or charge slips; there is no collection expense, and there are no losses from bad debts. The reduced expenses enable the store to sell at lower prices. The lower prices and the wider selection of goods attract customers and increase sales.

There are, however, disadvantages in selling for cash only. Many people with steady incomes do not have the cash when they need the merchandise and so they buy from a store which extends credit. Others wish to avoid the bother of paying for each purchase separately. They wish to pay for all purchases made during the month at one time. The store which sells for cash only may lose these two classes of customers.

The chain and other stores selling for cash only, however, have accustomed many people to paying cash. The store which sells for cash only may gain as many or more customers by its lower prices and wider assortment of goods as it loses by refusing to sell on credit. The fact that many stores in the past have sold on credit should not cause the new retailer to conclude that he must sell on credit. There is a place for both types of stores. The retailer should consider his location, the type of customers he has, the kind of goods he sells, and his available capital when deciding on the proper credit policy for his store.

Limited credit policy. There are few strictly cash stores. The so-called cash store may extend credit to government or private institutions, public utilities, contractors, and industrial companies. It also may extend credit for short periods to people known to be good credit risks. Some stores do not advertise that they extend credit but do extend credit to people who are good risks. Such a store does not encourage people to buy on credit, and informs those who do buy on credit that prompt payment is expected. This policy, which entails a small investment in receivables, may expand sales somewhat while keeping bad debt losses and collection expenses at a minimum.

Liberal credit policy. Some retailers increase their sales by extending credit freely. They may advertise: "Your credit is good"; "Terms to suit"; "Cash or credit"; or "Easy terms." Such advertisements encourage people with questionable credit ratings, people who can not obtain credit elsewhere, to come in and buy. If a store lives up to such slogans, it should expect to have a larger-than-average bad debt loss unless its collection procedure is very aggressive. The collection policy cannot be separated from the credit policy. The retailer who extends credit liberally must plan to follow collections closely. On the

other hand, retailers who sell only to the best risks can be less strict in making collections.

Sometimes the following statement is made: "98 per cent of the people are honest; so why not extend credit to all? You are going to lose on some accounts anyway." More than 98 per cent will pay promptly and voluntarily. The point, however, is not the assumption that 98 per cent of all of the people are honest, but whether 98 per cent of a store's customers are honest. The store that extends credit freely will find that much less than 98 per cent of its customers pay promptly. It will get more than an average share of customers who have been refused credit by other stores. Consequently, the store will face a serious collection problem created by many more than 2 per cent of the customers.

Liberal credit and small loss from bad debts. It is possible to extend credit liberally and to take only a small loss on bad debts. Many large stores extend credit liberally and lose only one-tenth of 1 per cent of total sales, or one-fifth or one-fourth of 1 per cent of their credit sales. Such a store does not advertise "Your credit is good," but it turns down very few applications for credit. It is a store for the masses and refuses credit to few people. How does it extend credit liberally and yet lose so little?

Every applicant for credit must go to the credit department and fill out an application, answering such questions as: Where are you employed? How long have you worked there? What do you do (occupation)? Where did you work previously? What is your address? Do you own your home? How long have you lived there? What were your previous two addresses? Do you have a bank account? If so, what bank? At what other stores do you have charge accounts? Give three references who are not relatives. The significance of these questions will be discussed later in this chapter.

While taking the application, the credit manager or one of his assistants has a chance to "size up" the applicant. If the information and the size-up are satisfactory, the account may be opened immediately, at least for small purchases. If there is some doubt, the applicant is asked to wait until the references

are consulted. A credit bureau may be consulted or the investigation made by credit department personnel or by the merchant himself. The applicant's employer may be consulted to verify the length of time employed, position, continuation of employment, and pay. If the applicant has charge accounts at other stores, the latter may be consulted to find how he pays his bills. Of course, the applicant may give only the names of the stores where he has good records, but even so one can learn much from these stores. The personal references may be consulted. If the information secured from these sources is reasonably satisfactory, the account is opened, and the applicant notified by telephone or letter. If not, when the applicant returns (if he does), he is asked to have one or two people guarantee the account. This procedure weeds out most of those who do not intend to pay. The information secured is also useful in making collections, as the customers who appear doubtful can be followed up very closely when they fail to pay on time.

Credit Problems of the Small Store

The small store. The small retailer may believe that he does not have the facilities to investigate credit applicants carefully. In most communities he can join, at a small cost, a local credit bureau and obtain most of the needed information from that source.

Retail credit bureaus number, perhaps, 1,200. They are found in most towns of over 10,000 population and there are several hundred bureaus in towns of less than 10,000 population. Many credit bureaus cover entire counties and so are prepared to serve the merchants in the smaller towns. City bureaus cover their metropolitan areas, including the suburban communities.

These credit bureaus gather credit facts about the people in their territories and pass them on to their subscribers. The bureaus have a system for exchanging credit information on people who move from one town to another, so that, in a relatively short time, a merchant can obtain information from his local

credit bureau about an applicant who has just moved into the community.

In operating a retail credit bureau the retailers of a community employ a manager and a staff to gather information for all members. This is quicker, more economical, and obtains more complete data than can be gathered by each retailer independently. When a retailer receives an application for credit, he can call the bureau, and, if the information on file is up-to-date, receive it immediately. If not, it will secure the information for him. Most bureaus give the information to the retailer and he makes his own decision; some attempt to rate customers. Even those which do not rate consumers may furnish opinions such as: "A department store reports that John Doe is good for a moderate amount."

One study of retail credit showed that the stores that subscribed for the reports of retail credit bureaus had a much lower bad debt loss than stores which did not. A study of over five hundred bankrupt concerns showed that 95 per cent did not belong to credit bureaus. The retailer who has available the services of a credit bureau should join the bureau and use its reports. Too often the retailer joins the bureau but only asks for reports on applicants when he is not busy. On busy days he often does not take time to check applicants for credit.

The village store has its own credit problems. It has frequently been said that the village merchant "knows all" about all the people in his community and hence can extend credit with a minimum of loss. It is an overstatement to say that the merchant knows all about all of the people in his community. Even in a small community, new people such as workmen or tenant farmers come and others leave. Moreover, the ability of people to pay changes from year to year. Therefore, the village merchant needs up-to-date information about his customers, too. If there is no credit bureau adequately serving his community, he should gather the information himself.

Some village merchants have said that if they extend credit to one, they must extend it to all—that they cannot discriminate among local residents, because those who were denied credit

would become antagonistic and the store would lose their trade completely. The fallacy of this position was expensively demonstrated during the depression of the 1930's. Many village stores failed because of numerous large, uncollectible accounts. The retailers who did not fail learned a lesson. Many of them henceforth extended credit only to responsible people, or set definite credit limits. When a family reached its limit, the store refused additional credit until a payment was made. One small town merchant who "never turned anybody down" switched to a cash basis just in time to save his business. He now points to a filing cabinet and says: "There are $35,000 of uncollectible accounts in there. I keep them just to remind me of my folly. Many of the people are still trading with me on a cash basis."

The farm supply store usually extends credit. Farmers generally expect credit until their crops are sold. The fact that credit is extended to some farmers, however, should not cause the small town retailer to feel that he must extend credit to everyone for as long as it is wanted. Many farmers can pay cash for their smaller purchases and they may be asked to sign interest-bearing notes for their larger ones. The point is that the merchant should not conclude that simply because he is located in a farming district he must extend long-term credit to all his customers. The chains have demonstrated that it is possible to sell for cash even in agricultural villages.

The manner in which a policy is carried out may be fully as important as the policy itself. If a retailer decides to extend credit to good risks only and to follow collections closely, he must decide which are the good risks and how best to collect without offending his customers. If a retailer decides to extend credit, he has several problems: passing on or refusing applications for credit; authorizing charge sales and keeping customers within their limits; and making collections.

The Credit Decision

A sound credit decision depends on factual information plus careful analysis. Imagination and ingenuity will help in getting information. Some sources, as mentioned earlier, include:

the customer; his employer; other retailers who sell to him on credit; his bank; his landlord; his personal references; legal records showing property owned, mortgages, suits and the like; and his neighbors. The simplest procedure is to have one credit bureau gather this information for a community and pass it on to the retailers.

Analyzing the application. Credit depends upon capacity, character, capital, and upon future economic conditions. By capacity is meant ability to pay. This is measured in part by the applicant's income as modified by the size of his family and their scale of living. A man with ability may be expected to increase his income and so become a good customer and credit risk even though his present income is small.

By character is meant willingness to pay. If a man is honest he will pay if he can. By capital is meant the property which the applicant owns. If the applicant owns property, a judgment may be obtained against him and eventually the debt may be collected. If the seller must bring legal action to collect an account, however, the expense probably will take all the profit out of the sale. So the retailer is more interested in the income and honesty of his customers than he is in the property which they own. Future conditions may greatly influence a man's ability to pay. If his place of employment closes, the customer loses his job and may be unable to pay. If the prices of farm products drop, the farmer's ability to pay is reduced.

Stated in another way, the credit rating of a customer depends upon the regularity of the applicant's income, the amount of his income, and his sense of responsibility. The regularity and size of income depend largely upon his occupation. A steady income seems to be somewhat more important in paying bills than a large income. Thus, office workers, school teachers, retail salespeople, and civil service workers usually are found to be good risks despite the fact that most of them receive moderate incomes. On the other hand, carpenters, masons, painters, plasterers, and coal miners may earn much higher wages but their incomes are irregular.

People in some occupations have a higher sense of responsibility than do those in others. Some people secure their posi-

tions through long years of work and cannot afford to lose them through negligence in paying their debts. Employers sometimes insist that employees pay their personal bills promptly. Some people seldom move from one community to another and so are very stable credit customers partly because they own property, a business, or because they consider themselves responsible members of the community where most people know them.

On the other hand, people are likely to be poor credit risks because of irregular work, low wages, or a poor sense of responsibility. Regardless of occupation, a man who has worked at the same job for many years is usually dependable and a good risk. The family that owns its home is usually responsible. The family that has lived in the same house for many years is established in the community. On the other hand, the family that has moved often is not necessarily a poor risk but the credit grantor needs more information. The man who has changed jobs frequently may be a good risk if he has been promoted each time, whereas the man who changes jobs often without promotions shows lack of stability. Before accepting the latter's credit, the grantor should obtain additional information.

The applicant's record of payment is important. Many retailers extend or refuse credit almost entirely on the applicant's payment record. If he pays his bills with reasonable promptness, he is considered a good risk. On the other hand, if he has had more than one account placed for collection, been sued for past-due accounts, or has had his wage garnisheed, he will probably be turned down by conservative credit grantors. Other information should be considered, but if it is lacking or inconclusive, the payment record he has established with other firms may be used in deciding to grant or refuse credit.

In analyzing the ability of a customer to pay, an important point to consider is his total outstanding indebtedness. The obligations which the applicant must meet from his income are a very important factor in determining how he will pay new obligations. This is also important when considering installment payments. Although a man's income may be ample to meet a payment of $20 a month, the fact that payments already

contracted for amount to $35 a month changes the situation. So in examining the payment record it is advisable to determine how much is already owed to others. The payment record and the total obligations of the applicant may be obtained through a credit bureau or directly from other retailers, professional men, and service businesses.

The size-up. When the retailer interviews the applicant for credit, he has an opportunity to form an opinion of the applicant's character and often of his ability. Some men are good judges of character and base their judgments largely on their opinion of the applicants. Retailers who are poor judges of character should not give too much weight to their opinion of the applicant's honesty and ability. It is much better to get information during the interview rather than to go "psychic" and follow hunches.

Securing information from the interview. In talking with the applicant the dealer has an opportunity to learn much about him: Where he lives—where he works—how long he has worked there—what he does—where he lived before coming to this community—whether or not he owns his home—how many members there are in his family—which of these are to be allowed to make charges—whether or not he belongs to a church—and if he is a member of a lodge or club. If some of his statements conflict, the retailer will become doubtful. Much information which apparently is not connected with credit may throw much light on the applicant's character and scale of living. Johns Hopkins made his fortune endorsing people's notes for pay. He very seldom was required to pay a note. Someone asked him how he judged people. He said that he watched people for two things: industry and thrift. If a man worked hard and lived within his income, he was likely to be a good risk.

The application form. All applicants for credit should be asked to fill out an application form. The small retailer may think this unnecessary for applicants with whom he is well acquainted. In fact, larger stores may open accounts for the best class of risks without this formality. But it is sound practice to ask everyone who applies for credit to fill out a form. The

dealer may be able to secure forms from his credit association; if not, he can prepare his own. The following is merely a suggestion and may be modified to suit the retailer's situation. It may be on letter-size paper or made to fit his record system.

APPLICATION FOR CREDIT FROM
(Name of Store)

Name:
(Mr., Mrs., Miss)..

Address..
Street Town

Telephone Number............... How long lived at this address?......... Do you rent or own?...........

Former address............................... For how long?........
Street Town

Name of (husband's*) employer......................... Address.......................
*If filled out by wife for husband Street

....
Town

How long worked there...................

Position......................... How long held?.................

Former employer....................... For how long?...........

Business references...

....

....

Personal references...

....

....

Do you have a bank account? Yes...... No...... Checking...... or Savings.....

In whose name is bank account?....................... Name of Bank............

Authorized buyers...

....
Letter Credit Limit (Signature)

Yes........

No........

Comments:

The space in the lower left-hand corner is for the retailer's judgment of the applicant; for this he may use a code. Next is whether or not a letter is to be written giving the retailer's decision. At the lower right is a place for the credit limit. This may be in code as C1 for $10, C2 for $20, C3 for $30 and so on up to $50 or $100. CU might be used to indicate unlimited credit. Sometimes it is desirable to set this limit with the applicant's knowledge. The applicant may be asked how much credit he will want and this may be set as the limit. In some cases, however, the retailer prefers to set the limit without the customer's knowledge. When a customer wishes to buy in excess of his limit, the dealer must again pass on his account. The limit may be raised or the credit may be refused. Sometimes the retailer will wish to interview the applicant again and secure up-to-date information from him and the other sources.

Failure to grant credit should not result in the loss of the customer. When a credit application must be refused, some retailers try to make the sale on a cash basis. Often this can be done successfully. The person with a poor credit record has probably been turned down before. In any event, he does not need to be angered by the refusal of credit. As an alternative to granting credit, the retailer may offer to hold the merchandise until the customer can pay cash for it. Some retailers do much business by weekly payments, delivering merchandise when payments are completed. In other cases the customer may be asked to have someone guarantee his account, or to give collateral security. If the article is durable and of large value, the retailer may secure a down payment, arrange installment payments, and retain title to the merchandise as security until all payments are made. If the applicant is found to be dishonest, the retailer does not want him as a credit customer; he may not want his business even on a cash basis and may decide to offer him no encouragement to patronize the store.

In refusing an application the dealer may say: "Until you have lived here longer and established your credit standing, why don't you pay cash?" Or, "Why don't you let me hold this until you have the money?" Or, the dealer may point out the advantage of a good credit rating and suggest that the applicant

should pay some of his present debts before incurring more. There are many tactful ways of refusing credit and not offending the applicant. Sometimes it can be done in a way to secure his goodwill.

Authorizing charge sales. To control the amount that is charged to an account and to prevent its use by unauthorized persons, it is necessary to have a system for authorizing charge sales. Large stores have a telephone or tube system for communicating with the office where charge sales can be checked against the store records to see that the buyer has an account and has not exceeded his limit. This is fairly simple when the purchase is to be delivered to the buyer's address as there is time to make the check before the package is loaded on the delivery truck. On "charge-takes" the situation is more difficult as it is necessary to identify the customer. If identification were not made, some persons would charge their purchases to the accounts of other people. Identification may be by an identification coin or tag issued to credit customers when the account is opened, by signature, by driver's license, or by the customer's general appearance of honesty.

For the store in the small town, authorization may be simple as the dealer knows the reputation of all his regular customers. In a larger store it is necessary to check the purchase (by telephone, tube, or a visit to the office) against the customer's ledger page, or the unpaid charge slips, or the credit file.

Making Collections

It has been pointed out that the collection policy should vary with the type of risks accepted as credit customers. If only the best risks are accepted, then the collection policy need not be aggressive. If poor risks are accepted, however, they must be followed up closely or losses will be high.

Large stores make a larger proportion of their sales on credit than do small stores. This may indicate that they use credit to increase their sales volume. Large stores also collect their accounts somewhat more quickly than do the smaller stores. Stores in small towns have about the same proportion of credit

sales as stores in larger towns but it often takes them much longer to get their money. This would seem to indicate that a larger proportion of the sales of small town stores are made to types of customers who, though good risks, are slow-paying, and that retailers in small towns are less aggressive in making collections. Long credit terms have been the rule in the one-crop agricultural regions such as the cotton areas in the South, tobacco areas in the Southeast, and grain areas in the Central West.

There would seem to be no reason for allowing the customer who is paid weekly or monthly three to six months to pay for small purchases. But this is often done because retailers believe that they must go along with the local custom or lose business. Some retailers in such towns, however, do collect their accounts more quickly than others and build goodwill while doing so. These towns need a community credit policy followed by all the retailers.

The first step in making collections is to have a clear understanding of the terms when the sale is made. If a farmer is to be allowed credit until he harvests and sells his wheat, this should be understood. If a working man is to pay on pay day, this should be definitely stated.

Collection procedure. The usual collection procedure is to mail a statement on the first of the month to all regular open-account customers. These statements are usually itemized. To save copying all the items, some dealers make their sales slips in triplicate and use copies for the itemized statement. One copy is given to the customer, one is kept by the store, and one is to be sent as a reminder that payment is expected. Some retailers even make charge sales slips in quadruplicate so that two itemized statements may be sent.

If payment is not received it is customary to send a second statement at the middle or end of the following month. The retailer or his bookkeeper checks over all accounts semi-monthly or monthly and mails follow-up statements to all those who should receive them. Of course, if a credit period of more than 30 days has been promised, statements will not be mailed at the end of the month. If ledger sheets are used, the dates and terms

of all purchases and all payments will be shown. If sales slips are used, they will show due dates; those remaining in the file will be checked every month or oftener and statements mailed.

If payment is not received within 15 days after the second statement, the account may be considered delinquent or a third statement may be sent. The second or third statements often have a written message such as "Please remit" or "Prompt receipt of your check will be appreciated." Red stickers may be attached to call attention to the fact that it is the second or third statement, or that the bill is past due.

When customers are considered delinquent they should receive special attention. Any or all of the following collection methods may be used with past-due accounts: collection letters, telephone calls, personal calls, collection agencies (perhaps the collection department of the local credit bureau), lawyers, and suits or garnishment of wages.

The collection manager should have a definite system for following up his delinquent accounts. This requires a tickler system which uses a copy of the statement or bill or invoice as a basis of the system. Every time a collection letter is sent, this action is noted on the statement, which is then placed in a folder to come up for attention on the desired date. For example, if a letter is written on the 10th and ten days is a reasonable time for a reply, the statement is placed in the folder for the 20th. If payment has not been received by the 20th, another letter is sent or some other action taken. When the man is reached by telephone he may promise to come in and pay; a note is made of his promise and the statement placed in the proper folder. If he does not come in on the promised date, further action must be taken. A personal collector may report illness and a request for an extension of time; if this is granted, the invoice is placed in the proper advance folder.

Collection letters are frequently used in trying to collect past-due accounts. The retailer often can obtain a set of letters from his credit bureau if he does not wish to write his own. He should change the set occasionally so that if the same customer becomes delinquent a second time, he will not receive the same

letters. Some of these letters obtain good results. Letters are a good way to reach rural customers who can not be contacted easily in person or by telephone. It seems, however, that a retailer should not use more than two or three in a series on his delinquent customers.

The telephone is sometimes more effective than a collection letter. If the debtor can be reached by telephone, this may be a very productive and relatively cheap method of making collections. If the debtor has no telephone at home, he may be called at his place of work. This should be used only in more serious cases. The retailer can not collect over the telephone but he can induce the debtor to come in and pay or make a definite agreement as to when he will pay. Under some conditions it may be desirable to ask the delinquent customer to visit the store; the fact that his account is overdue is not discussed on the phone.

Personal collectors are frequently used in making retail collections of both delinquent open-book accounts and installment accounts. The small retailer may have one of his salesmen go out and make collections at times when he is not needed in the store. The larger store may have one or more men who devote full time to making collections.

Collection agencies are the next step. The local credit bureau may operate a collection department and all delinquent accounts may be turned over to it. The bureau will send out notices, letters, and personal collectors, and if these fail it will have a lawyer bring legal action. The debtor may be sued. If he is employed he may have his wages garnisheed. If he has a bank account or other property in the hands of a third party, it may be possible to garnishee this or obtain a judgment and levy on it.

Unless the retailer has a credit manager, or unless he himself has the time and knowledge required to handle his delinquent accounts, it is best to turn them over to a collection agency. Most towns have local collection agencies. In the smaller cities the agency is often a one-man business. The retailer should select his agent with care because the latter have been known to make collections and keep the money. Lawyers will often act

as collection agents. In many towns the retail credit bureaus also operate collection departments.

Frequently the embarrassed debtor simply ignores statements and letters. When the collection agent contacts him, he may discover that there is a legitimate reason for the delay. In such cases an extension may be arranged. When a debtor is involved with a number of creditors, all of them may turn their accounts over to the credit bureau so that the debtor has in effect one account to pay. The bureau advises him and helps him work out his difficulties. As it collects the money, the necessary amounts are turned over to the various creditors.

Installment Credit

Many hot debates have raged over the merits and demerits, the soundness and the dangers of installment selling. We have little space to review them here. In general, experience has proved installment selling to be safe when properly used. A few facts should, however, be mentioned to help in the understanding of installment credit and its legitimate uses.

First, many people cannot buy large articles (such as automobiles, refrigerators, washers, trucks, tractors, stoves, overcoats, furniture) and pay for them in 30 days out of current income. We may argue that people should save their money and pay cash for their large purchases. We can point out that it is economical to do so, but many of them will not do so. Many people need money *now,* for example young married people setting up housekeeping and young men going into business or farming.

Second, installment selling extends credit safely to a poorer class of risks than can be sold on open account. Credit risk is lessened since payments are scheduled periodically and the goods are used as security for the loan until payments are completed.

Third, the down payment (cash or trade-in) should cover the initial depreciation which occurs when an article is first put into use and thus becomes a "used" or "second hand" article. The payments, whether monthly or weekly, should run ahead

of the depreciation even under hard usage. If they do, most buyers will "pay out."

In the past, installment credit charges were high. These charges cover not only interest on the money involved, but the expenses of keeping records and making collections, the cost of making repossessions, and the loss on resales. Buyers usually did not or could not determine the actual rate of interest they were paying. They thought only of the cost of the credit. If an individual wanted a refrigerator but was $100 short of the purchase price, the seller might say that the carrying charge would be $10 for 10 monthly payments of $10 each. To the buyer, the $10 looks like a small addition to the cost of the washer. Yet the money is paid off in monthly installments and the average time the money is outstanding is approximately 5½ months, so the actual rate computed as simple interest is 21.8 per cent. This rate may not be excessive when the cost of handling the sale is considered, but it is probably more than the customer realized when he signed the contract.

As finance companies and banks found installment notes to be safe and competition between them increased, finance charges declined. Formerly, rates of 30 to 50 per cent were common. More recently rates over 30 per cent are unusual whereas rates of 10 to 30 per cent are common. If the costs of making collections, bookkeeping, and bad debt losses are not too high, installment notes still offer a satisfactory rate of return.

The retailer with the necessary funds may carry his own installment paper or he may arrange with a finance company or a bank to buy the notes from him. He naturally prefers to sell the notes without recourse to him for payment. If he has established his reputation as a conservative operator, one who checks his risks carefully and requires reasonable down payments, he can often do this. When the dealer sells his installment notes he usually agrees to repair and resell any merchandise which must be repossessed.

Contracts. A retailer should consult his credit bureau or a competent lawyer as to the contract to be used. It may be that a conditional sale, chattel mortgage, or bailment lease will be used. State laws vary; thus, local advice is needed. Perhaps a

contract form can be secured from the local credit bureau. If the retailer sells his notes to a finance company, it will supply the contract form to be used.

Records. If the retailer keeps his installment notes and col-

RECORD OF INSTALLMENT PAYMENTS

Name.................................... Account Number.........

Address.................................... Date and Article (3/1 washer)

.... Terms ($10 mo. on 1st)

Date and Article.................................... Terms ($5 mo. on 10th)

Date	Sales	Payments	Balance	Past Due	Remarks
Mar. 1	$120		$120		
Apr. 1		$10	110		
May 1		10	100		
June 1		10	90		
10	50		140		
July 1		10	130		
10		5	125		
Aug. 1		—		$10	
2					
10		—		5	
11					
Sept.					

lects from the purchaser, he will need a book or set of cards on which to keep the necessary information. The records should call attention to past-due accounts promptly so that they can be followed up quickly. The buyer may be given a card or book in which all his payments are entered, and this serves as his receipt. The dealer may prefer a form which may be prepared by his accountant to fit in with his general accounting system. If he has no accountant, he can buy standard forms at stationery stores. If he uses a bookkeeping machine, the manufacturer of the machine may help him set up a system suited to his business to which the machine is adapted.

A separate card or sheet may be prepared for each purchase, or all current installment accounts owed by a customer may be carried on the same sheet. The accompanying form shows one type which is used. It provides space for several purchases with the terms in each. "Add-on" is the term used to describe the situation when a customer buys another item before payments on the first purchase are completed. Usually the new item is added to the old contract and the new payments added on the other payment. When a sale is made, the bookkeeper heads a sheet and writes the dates payments are due. Payments are entered as made and the balance carried forward. As soon as a payment is missed, the sheet can be pulled from among the regular accounts and placed with the delinquents for special collection efforts.

Installment collections. Sellers usually prefer to have installment buyers come to the store to make payments. They may see other things they want and, as their contracts "pay out," the salesmen have the opportunity to sell them additional merchandise.

Payments may be due monthly, semi-monthly, or weekly and prompt action should be taken once a customer has missed a payment. If a customer gets far behind he often has difficulty in catching up; the seller, meanwhile, has considerable expense in making the collection and may have to repossess the goods. To lessen the danger, the dealer should follow up all past-due payments quickly. The customer may be called on the telephone, or sent a written notice. If this does not bring in the

money, or a reply, a personal collector should visit the customer at once. Installment collections must be pushed hard. If a dealer is not prepared to make collections in this way, he should stay out of the installment business or turn his paper over to a finance company which makes collections.

Credit Control

The retailers in many communities have set up what are called community credit policies. Under these policies they exchange credit information, agree upon down payments and number of monthly payments, and in some instances agree to charge interest on open accounts after they are perhaps 60 days past-due. One thing which retailers watch closely is their collection percentage.

The collection percentage is computed by dividing the amount of receivables on the books at the first of the month into the amount collected during the month. If a merchant has $10,000 in receivables on his books the first of the month and collects $6,000 on accounts during the month, his collection percentage is 60 per cent. Obviously, to be accurate, collections on installment accounts should be computed separately. To make this computation the dealer should record separately his receipts from cash sales and his receipts on charge accounts; and if collections are made on installment sales, the amounts should be recorded separately from those on open accounts.

As a merchant watches his collections and those of other merchants he may find that 60 per cent is a good average or standard. If he pushes his collections hard, follows up slow customers with letters, telephone calls, and personal collectors, and collects 70 per cent, he may be creating ill-will and find it advisable to ease up a bit and not push his customers quite so much. He may reason: "If 60 per cent is a good average, why go above it and drive customers away?" If, on the other hand, he becomes lax in making collections and lets his percentage drop to 50, the indication is strong that he should be a little more aggressive, and he may say: "If the other store collects 60 per cent, I can do as well. Why have so much money tied up in receivables and increase my bad debt loss?"

The average number of days it takes to collect accounts is another method of measuring the efficiency of credit operations. The number of days can be computed by dividing 30 (the number of days in a month) by the collection percentage and multiplying the result by 100. Thus if the collection percentage is 60: $\frac{30}{60} \times 100 = 50$, the average number of days it takes the store to collect its accounts.

Another method is to divide the average amount of the accounts receivable by the average daily charge sales. If a store has $10,000 in accounts receivable on April 1, makes $6,000 charge sales during April, and has $11,200 on its books on May 1, then the average receivables on the books is $10,600 ($10,000 + $11,200 ÷ 2). The average daily charge sales are $200 ($6,000 ÷ 30). Then $\frac{\$10{,}600}{\$200} = 53$ days to collect.

Adopting a standard. The retailer should adopt standards to guide him in granting credit and making collections. He may decide the proportion of his total sales that should be made on credit, and the amount of money which should be tied up in accounts. He can then solicit sales on credit or refuse credit as the situation demands. He can be more aggressive in making collections if his percentage decreases (the number of days outstanding increases). Or, if his collection percentage seems too high, he can relax his collection efforts somewhat. The dealer can compute his collection percentage (or the number of days to collect) each month and plot it on a curve. By showing these facts graphically he can readily compare one month with another and the current year with previous years.

Sales and collections are likely to have seasonal peaks and valleys and the retailer should allow for these in setting his standards. He should also make allowances for changes in economic conditions. When conditions are bad, he may be more aggressive in making collections in an effort to obtain his money ahead of other retailers. Or, he may decide that his customers can not pay and change his collection policy accordingly.

Credit can increase sales and profits. The retailer sells on credit to increase his sales and profits. Poor collections do

neither. Actually a close collection policy may increase sales. Let us suppose that two retailers, Jones and Smith, have stores in the same town. Jones is lax in making collections while Smith is strict. In this town Mr. John Doe owes Jones a large bill which is long past due. He owes Smith nothing as Smith kept after Doe and keeps the account paid up-to-date. Suppose John Doe finds that he must have a new suit. Which one will Doe patronize? If he goes to Jones, he may be turned down. In any event he is sure to be asked to pay his account. But if he goes to Smith he knows his record is clear and that he will have no difficulty in getting the suit on credit. So Smith makes the sale while Jones must still collect his long past due account.

Good collections get the money and keep the customer. The retailer must collect his money if he is to stay in business. On the other hand he must keep his customers if he is to survive. If he is too slow in making collections he will have too much of his capital tied up in accounts receivable. He must collect his money with reasonable promptness, or he must charge higher prices for his goods, if he is to maintain or increase his profit. A strict collection policy followed fairly, courteously, and tactfully can increase sales and profits.

New accounts. Offering credit service gives a store the opportunity to solicit business from new customers. The retailer or his credit manager can compile lists of good credit risks, and open accounts for them even though they are not customers. They may be notified by letter that accounts have been opened in their names and invited to come in and use them. Or, their names may be given to outside salesmen who visit them to make sales or just to get acquainted and build goodwill.

The retailer selling on the installment plan should keep close contact with customers. Those who keep up their payments may be good prospects for other sales. When their accounts are nearly paid, their names may be given to salesmen, who will attempt to sell them more merchandise. Sometimes retailers notify such customers that they can make additional purchases without making another application for credit. Both techniques may be used in dull periods to increase sales.

When these customers are allowed to make purchases without any down payments, they are being treated as open-account buyers insofar as the down payment is concerned. Some retailers may also select customers who have established good records in paying for installments and offer them regular credit accounts.

Questions

1. What are the three credit policies which a store may adopt?
2. What are the advantages of operating on a cash basis? Disadvantages?
3. What can a credit bureau do for a small retailer?
4. How does a retail credit bureau operate?
5. From what sources may a retailer obtain information which will aid him in making a credit decision?
6. Upon what general factors does credit depend?
7. What information should be obtained during a credit interview? What is the significance of the various facts which are requested on an application form?
8. How are charge sales authorized?
9. How does the credit policy affect collection policy?
10. Describe a collection procedure.
11. What methods may be used to collect delinquent accounts?
12. How much should the down payment in an installment sale be?
13. What is included in the cost of installment credit?
14. What records of installment sales should a retailer have?
15. Why is it preferred that installment buyers come to the store to make payments instead of mailing them?
16. How may a retailer's collection efficiency be measured?
17. Why do retail grocers collect their accounts more quickly than retail clothing stores? Why are groceries not sold on the installment plan?
18. It is said that a firm collection policy builds sales; that a person tends to buy from the store where he knows his account is paid and his credit is good; and that he tends to avoid the store where he knows his account is long past due. Is this true? Comment on the statement.

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Record Keeping

RETAILERS often question the necessity or value of keeping records. They express their views as follows: "Why keep a lot of complicated records? I can see what's going on in my business. I'm here every day. Anyway, I'm too busy running my store. I don't have time for keeping records. Besides, I don't know anything about it."

Neither a large number of records nor complicated records are necessary. A set of useful records can be simple, easy to keep, and will require relatively little of the retailer's time. Many of the unsuccessful and bankrupt retailers are found to have had poor records or no records at all.

Why Keep Records?

Numerous studies by the Department of Commerce and others have shown that most small stores that fail either have inadequate records or none at all. Business success and good record-keeping seem to go hand in hand. If it is true that an adequate record-keeping system would help to reduce the probability of failure and increase the chances of survival, that alone would be a sufficient answer to the question, "Why keep records?"

How does the keeping of records decrease the chances of failure and increase the chances of a dealer staying in business and earning a profit?

This can best be answered by listing some of the types of

information that a record system can furnish. A simple but adequate system can supply the information needed to answer the following questions:

How much business am I doing? How much are my cash sales?

How much are my credit sales?

How much gross margin do I earn?

How much are my expenses, including non-cash expenses?

How much net profit (if any) am I earning? How much income taxes will I have to pay?

What is my net worth?—that is, what is the amount of my proprietorship in the store?

What are the trends in my sales, expenses, profits, net worth, etc.?—that is, how is my store progressing from year to year?

How much stock (inventory) do I have on hand?

How much merchandise do I take out of my store for personal or family use which I do not consider as sales?

How much money do I owe my wholesalers and others?

How much am I collecting on my credit business?

How much do my customers owe me now (both current and past due)? Can my business stand this much?

How much cash do I have on hand and in the bank? Is this the amount I should have on hand?

How does my store compare with other stores in the same line of business?

With answers to such questions available, the retailer knows WHEN something is wrong, he knows WHERE that unfavorable condition has developed (whether in sales, collections, turnover, expenses, gross margins, etc.), and he is in a position to do something about unfavorable conditions before his store is forced out of business.

In a study of retail management practice made by the Department of Commerce, it was found that, among the stores surveyed, most of the profitable ones kept good records, whereas most of the unprofitable ones kept poor records. "It is not surprising that 83 per cent of the profitably operated stores kept up-to-date accounts, that 88 per cent of them kept neat and orderly books. . . . Compare these percentages with those for unprofitably operated stores—40 per cent and 47 per cent. . . . Poor bookkeeping appears to be a decidedly large factor in the unsuccessful operation of a business."

Good records not only help a retailer to operate a store profitably and successfully, but also retailers who have successful businesses usually recognize the benefits of good records. Aside from the business value of records, the Federal income tax regulations, the Social Security Act, sales tax laws in many of the States, and an increasing number of other tax laws and regulations require certain records and reports. In short, record keeping is necessary because records increase the chances of survival of new stores just starting in business; they increase the chances of earning profits by established stores; they are increasingly necessary for various tax purposes.

Sales Records

There is one record that almost every retailer is interested in keeping. No matter how few records are kept, he wants the answer to the question: "How much business am I doing?" When this record is kept, how is the information used?

The benefits of sales records are obtained by making comparisons. The dealer can compare this month's, this week's, and even this day's business with the sales of the corresponding month, week, or day of some previous period to find out in what direction his sales are moving. If his sales begin to fall off, he knows it immediately. He has the facts and can then search for the cause or causes and start to correct the situation before it gets out of hand. If the sales trend is upward, he can discover why his sales have increased. The reason may indicate the practices to follow or the merchandise to push in the future.

Sales records help the retailer to determine the results of his advertising. The cost of the advertising and other types of promotion can be compared with his volume of business.

Every retailer obtains higher margins on some lines than on others. Without sales figures for his various lines, a retailer will not know if his low-margin lines are accounting for a dangerously large share of the store's total sales. When this happens, the total gross margin of the store may not even be sufficient to cover expenses. Advertising, store or window dis-

plays, or outside salesmen may be used to increase lagging sales of the higher-margin merchandise. The facts, however, must be known before a decision can be made to try special sales efforts, or to play down or close out the articles.

Records should show sales and gross margins for each department. These amounts can then be compared with the expenses of each department. To obtain this information, a record of sales by lines or departments can be kept in one of the four following ways:

1. Write down sales in separate columns. Some stores use a sheet of paper with a column for each major line. This is kept beside the cash register. Before ringing up a sale, the salesman enters the sale amount in the proper column. When this method is used, vigilance is necessary to insure that salespeople record each sale.

2. Departmental keys on cash registers. The cash register may be used to obtain departmental sales figures. When a sale is rung up, the key showing the amount of the sale is pressed and the department key is pressed to record the department making the sale. Each department's sales are recorded separately and added separately by the cash register. At the end of the day the retailer opens the register and reads the total for each department. When the salesperson writes out sales slips for charge sales, he must ring up these slips by department on the cash register in order to get charge sales into the departmental totals.

3. Cash register tape. Some cash registers do not automatically provide departmental totals, but they do give the retailer a printed record on a strip of paper which shows the amount of each sale, and the code symbols of the department making the sale. This cash register tape is then re-added by departments: all sales of tools are totaled, then sales of paints, and so on.

4. Separate cash registers. A fourth method is to provide a separate cash register for each department. Daily or weekly sales totals must then be entered in a summary record.

Sales on credit. For credit sales a customer duplicate-statement ledger with binder and a set of customer sales tickets may be used. The invoice has a space for balances brought for-

ward; each purchase is entered on both original and carbon. The original is sent to the customer at the end of the month as his statement and the carbon is kept as the store's permanent record. Under this system, entries on the combination invoice and ledger are made from the sales ticket. The sales ticket or a carbon copy of it is taken from the salesman's sales book and filed with the ledger or in a separate file.

Some retailers prefer a sales ticket made in triplicate or quadruplicate. A carbon is given to the customer with each purchase, the original is sent at the end of the month as a statement, and one is kept by the store until the bill is paid. If made in quadruplicate, two itemized statements may be sent to the customer.

Under some systems the original sales ticket is given to the customer when the bill is paid and the store retains no copy for use in preparing sales promotion mailing lists. If this is the method used, the store should develop some other system of recording names and addresses of customers together with the dates when large or expensive articles were purchased. This record, which should also include the merchandise name, is particularly important in the sale of merchandise that will need servicing and supplies that must be replenished frequently.

Purchase Records

Some stores use a register to give a complete record of all purchases of merchandise showing all charges, credits, cash discounts, and allowances. The initial entries on the invoice and margin register are usually made from the actual invoices. A separate page is set up for all firms from which frequent purchases are made, and a miscellaneous sheet is set up for a record of invoices from scattered sources. As invoices are paid a notation is made on the invoice register.

This record usually provides spaces for the amount of the invoices, terms (credit period), cash discount allowed if paid by a specified date, credit allowed the store, and freight or express allowed. From these columns the net amount to be paid is computed and entered.

INVOICE AND PURCHASE REGISTER

DATE 19—		NAME OF SUPPLIER	DATE Due	DATE Paid	TERMS	AMOUNT OF INVOICE		RETURNS AND ALLOWANCES		DISCOUNT		AMOUNT PAID	
Jan.	3	Brown Bros.	1/13	1/13	2/10, n/30	352	61			7	05	345	56
	6	Smith & Jones	2/5	2/5	n/30	421	09	15	21			405	88
	10	Green & White	1/20	1/20	1/10, n/30	215	32			2	15	213	17

In some registers there are additional columns for determining the markup. In case the retailer must pay freight on a shipment, this charge is added to the amount paid the seller in order to determine the total cost to the buyer (i.e. the retailer). Then the total selling price is entered and the difference, which is the dollar markup, computed. The last column allows space for recording the percentage of markup. This initial markup will be the margin if there are no markdowns and no lost goods or stock shortages. Many retailers, however, do not care to compute the percentage of markup on all purchases. In the case of a job lot consisting of numerous, assorted articles it is desirable first to compute the estimated total selling price of the lot and compare it with the cost price to ascertain if there would be a sufficient margin to justify the purchase of the lot.

If the retailer wishes to record his purchases by departments, he can allot a separate column in the register to each department. As invoices are received, the purchase is entered in the proper departmental column and any freight and cartage amounts can also be added. The totals of the columns show purchases by departments and can be used by the department itself, and by the proprietor in making comparisons.

Cash Records

Did you get all the money that customers spent in your store today? Were there errors in making change? Did some customer walk out of the store without paying his bill? To be able to answer "no" to these questions requires that proper safeguards be established in the store operation and organization plan. Record keeping can help by disclosing the presence of such leaks, but the prevention of their occurrence is primarily a problem of management.

Serious problems arise in connection with cash shortages. The most obvious is that the retailer has lost money. Another is that when there is a loss of cash, real or imagined, all those who have handled the cash feel the shadow of suspicion upon them. The retailer should safeguard his cash properly.

One of the primary purposes of cash registers is to protect the retailer's cash. Some makes provide separate cash drawers for each clerk, itemize and total each sale, show the amount of the transaction at the top of the machine, and may print and deliver a receipt to the customer. Since for every customer transaction the description and the amount of the sale will appear at the top of the register, a bell will ring, and a ticket will be printed (on some registers), it is not likely that a clerk would ring up a dollar sale as one for only 75 cents. Thus, the cash register eliminates or minimizes several of the causes of cash shortages.

Another safety measure is to insure that all the money taken in is either deposited in the bank or is accounted for by signed paid-out slips. Each day the owner should take the cash re-

ceipts for the day and deposit the exact amount in the bank (leaving only the regular change fund in the cash register). If the receipts were $200.04, a deposit should be made for $200.04, not $200.

A deposit of the exact amount of cash received simplifies the problem of safeguarding and checking the cash. The retailer has a daily record of his cash-register reading; he records the daily total in his record and at the end of the month he receives a bank statement which again shows these identical amounts in the deposit column.

Daily proof of cash. A daily proof of the cash on hand can be made as follows: The retailer writes down what was on hand in the morning, adds to that the day's receipts (as shown by the cash register), subtracts the paid-outs as per the slips, and the result is what should be on hand. If it is not, there is a shortage in cash. The shortage may result from any number of causes, and perhaps one should not expect to eliminate every penny of cash shortage. Every effort should be made, however, to determine where or how it occurred in order that similar losses may be prevented in the future. If the shortage occurs in the same place too frequently, it means that something needs to be corrected. It may be due to carelessness or it may be due to other causes, such as petty theft.

If a cash shortage is discovered, the retailer should make an investigation immediately. This means that the cash should be checked every day. The following form can be used in making a proof of cash on hand:

1. Cash on hand last night	$ 25.00
2. Total cash received today (as shown by cash register readings)	176.25
3. Total (1 and 2)	201.25
4. Less: Cash paid out today (as shown by paid-out slips)	6.25
5. Cash which should be on hand (3 minus 4)	195.00
6. Actual cash on hand (count)	194.75
7. Cash short (or over) (5 minus 6)	$ 0.25

In making the daily proof of cash many retailers count the change fund and set it aside. That is, they do not include it in

"cash on hand last night" (item 1). When the dealer follows the practice of depositing the exact amount of the day's receipts in the bank, the only cash on hand from last night will be the change fund.

When the bank deposit is made in the middle of the day or does not include the day's total receipts, it becomes necessary to make a provision in the above form for deducting the bank deposit as well as the "cash paid out." Another line should be inserted between items 4 and 5, reading: "Less cash deposited in bank today."

Recording Systems and Reports

There are many systems of record keeping but it is beyond the scope of the present treatment to offer more than a brief discussion of some aspects of record keeping. Some retailers employ outside accountants who install systems and drop in daily, weekly, or monthly to post their books and make up their various tax and operating statements. The retailer need only keep records of cash and charge sales, bank deposits and bills paid and allow the accountant to keep the books and make up whatever statements must be made up for tax payments, the bank, other creditors, and the retailer.

If one is not familiar with the elementary principles of bookkeeping, his effort and time will be well rewarded by enrolling in a night school, college, or correspondence course. Some would go so far as to say that a retailer is inadequately trained for his vocation if he has not mastered the principles of double-entry bookkeeping.

Profit and loss statement. The profit and loss report or operating statement is a summary of the operations for a given period, usually a year. It summarizes the operations as follows:

$$\text{Sales} - \text{Cost of Goods} = \text{Gross Margin}$$
$$\text{Gross Margin} - \text{Expenses} = \text{Net Profit.}$$

In the accompanying statement, cash discounts taken on purchases were deducted from the purchases. If this is not done,

such discounts should be included in "other income," and added to the operating profit to obtain the net income. Net sales are taken as 100 per cent in the computation of all percentages except percentages of earnings or income on capital. This procedure is a very general custom.

FORM OF PROFIT AND LOSS, OR OPERATING, STATEMENT

		DOLLARS	PERCENTAGES
Gross sales	$63,660		
Less returns and allowances	3,660		
Net sales		$60,000	100.0%
Inventory (goods in stock) Jan. 1	$16,000		
Purchases: $37,390 plus transportation on goods of $660	$38,050		
Cost of goods handled	$54,050		
Inventory, Dec. 31	$14,450		
Cost of goods sold		39,600	66.0
Margin		$20,400	34.0
Operating expenses:			
Salaries and wages	$10,140		16.9
Rent	2,700		4.5
Advertising	1,560		2.6
Loss from bad debts	150		.25
Insurance on stock and fixtures	270		.45
Taxes on stock and fixtures	360		.6
Interest on investment, excluding building	1,380		2.3
Other expenses	2,400		4.0
Total, including interest		$18,960	31.6
Operating or net profit		$1,440	2.4
Other income		660	1.1
Net income (or profit) over and above interest on investment		$2,100	3.5
Net earnings or income, including interest on investment		3,480	5.8
Net earnings or income on capital			12.3%

The financial statement or balance sheet. This statement is a summary of the property owned by the retailer, the debts he owes, and his equity in the business. The property owned is usually only that used in the business and is called the *assets* of the business. The debts likewise are those of the business

and they are called *liabilities*. The difference between the sum of the assets and the sum of the liabilities is the owner's *net worth* or *equity* in the business. In other words, assets minus liabilities equals net worth.

In making up the balance sheet it is customary to list the assets on the left-hand side of the page in the order of their liquidity. Assets are "liquid" or "quick" if they can be converted quickly into cash. Cash is the most liquid asset and appears at the top. Accounts and notes receivable come next (unless the store owns marketable securities), followed by inventory. Then follow the fixed assets: furniture and fixtures, delivery equipment, and land and building if owned. Similarly, on the right-hand side, the debts which must be paid first are listed first and those payable later follow in sequence according to their due dates. The following is the form of a conventional balance sheet:

ASSETS			LIABILITIES	
Cash: on hand	$ 100		Accounts payable	$2,400
in bank	2,200	$2,300	Notes payable	1,700
Government bonds		1,000	Total current liabilities	$4,100
Accounts receivable		4,000		
Notes receivable		1,000	Net worth	
Inventory (stock)		10,000	(Proprietorship Account)	17,200
Total current		$18,300		
Furniture and fixtures		1,500		
Delivery equipment		1,500		
Building (rented)		——		
Total fixed assets		$ 3,000		
Total assets		$21,300	Total	$21,300

It is customary in analyzing financial statements to consider total assets to be equal to 100 per cent. Then relative changes in the individual assets and groups of assets can be compared from year to year. Liabilities and net worth can be compared relatively with each other and with the assets.

Departmental Accounting

The profit and loss statement informs the retailer of his total store profit for a given period. Some retailers desire more

information, however, especially when they handle numerous lines of goods carrying different margins and varying expenses. Some merchandise lines, or store departments, divisions, or groups of departments may be profitable while others are handled or operated at a loss. It is desirable to know which are profitable and which are not. Or, to state it another way, which are most profitable.

To determine sales and gross margins is not difficult. Gross margin is the difference between total sales and total cost of the goods sold. It is determined by adding the value of the opening inventory to the purchases and deducting the value of the goods on hand at the end of the period. For example:

Sales of Dept. A....................		$10,000
Inventory Jan. 1........	$ 2,000	
Purchases during year....	9,000	
Goods on hand.........	11,000	
Inventory, Dec. 31......	3,000	
Cost of goods sold	$8,000	8,000
Gross margin......................		$2,000

This procedure is simple and generally understood. Most retailers can, with little or no extra work, determine the gross margin on their various merchandise lines if they keep a record of sales and purchases by departments. The methods of recording the sales by lines have already been outlined (see pages 462-463). Furthermore, inventories are usually taken by lines or departments, which also simplifies the departmental accounting procedures.

A retailer does not need to keep departmental records or allocate expenses in order to have an adequate accounting system. He may start with a simple system and add the departmental records later. He may desire to record his sales, purchases, and expenses by lines or departments for only a portion of the store or for only a part of the year. Although these records do not furnish complete information, they may be adequate to guide him in making policy decisions.

Some facts are necessary, however, to serve as a basis in mak-

ing decisions. For example: to advertise certain lines or to push the sales of some departments; to add certain lines or to discontinue others; to judge the results of previous decisions. Changes occur and from time to time a background of facts is needed in order to adjust business operations to changing conditions and circumstances. Such guidance can come from detailed and reasonably exact accounting information, estimates, or data gathered during test periods, and close and careful observation of the business.

Allocation of expenses. For purposes of illustration let us assume that a certain hardware store is divided into five departments designated as Departments A, B, C, D, and E. A profit in one department can easily be lost in another without the owner realizing it. Sales, cost of goods sold, and margins are determined for each department by keeping the above-mentioned departmental records. The next problem is to distribute expenses accurately to these five departments. The proper proportion for each may be allocated in various ways.

The retailer watches his own activity for a test period and determines, for example, that one-half of his time is devoted to Dept. A, one-sixth to Dept. C, and one-sixth to Dept. E, one-twelfth to Dept. B, and one-twelfth to Dept. D. His salary is distributed on this basis in the accompanying table.

The salesmen are paid on a commission and drawing-account (salary) basis and their earnings are distributed to departments in the proportion in which their commissions are earned.

Alterations and repairs are made on some merchandise in the workroom. Some merchandise is also processed in the workroom before it is offered for sale. Work tickets are kept by departments and the cost is distributed directly to the department for which the work is done.

Relatively more time is spent, in proportion to sales, in sending out statements and recording payments for Dept. A than for Dept. E. An analysis of how the bookkeeper's time is spent is therefore made. The distribution of time shown is based on this study. Although it may not be entirely accurate, any errors would have very little effect on the final results as her salary is a relatively small part of total expenses.

Traveling expenses are divided on the basis of sales. No attempt is made to separate the buying trip expenses from other necessary traveling expenses for the business since buying trips are frequently combined with other necessary business trips.

Advertising is charged to those departments which use it. If merchandise from several departments is featured in the same

TABLE 28–1

DEPARTMENTALIZED PROFIT AND LOSS STATEMENT

	DEPARTMENTS					
	Totals	Dept. A	Dept. B	Dept. C	Dept. D	Dept. E
Sales	$175,000	$110,000	$12,000	$10,000	$25,000	$18,000
Cost of goods sold	135,200	92,000	9,500	8,700	17,000	8,000
Gross margin	39,800	18,000	2,500	1,300	8,000	10,000
Expenses:						
Labor:						
Owner's salary	3,000	1,500	250	500	250	500
Salesmen	6,900	4,000	600	900	1,200	200
Office	905	400	50	50	125	280
Workroom	4,600	2,900	100	250	750	600
Total labor	15,405	8,800	1,000	1,700	2,325	1,580
Traveling expense	2,500	1,573	170	145	355	257
Advertising	1,900	425	—	200	—	1,275
Bad debt loss	900	47	153	198	302	200
Delivery	1,100	700	100	100	100	100
Occupancy	4,000	2,050	410	76	770	694
Insurance—stock	300	90	48	24	108	30
Insurance—equipment	120	60	18	10	20	12
Insurance, pub., empl., auto., and contractor's liability	360	135	23	22	45	135
Taxes	350	100	40	20	90	100
Interest	2,100	601	239	119	540	601
Miscellaneous	1,200	754	84	68	170	124
Total expenses	$30,235	$15,335	$2,285	$2,682	$4,825	$5,108
Profit or loss	$ 9,565	$2,665	$215	L1,382	$3,175	$4,892

advertisement, the cost may be prorated among them on a space basis. In the case of this store, Depts. B and D used no advertising in the period being studied. Advertising for Dept. E was done on trade-ins or parts. Dept. E used newspaper and direct-mail advertising to the extent of $1,275. In proportion to sales, more was spent on advertising for Dept. C than for Dept. A. The retailer was trying to increase the sales of Dept. C in the belief that the department was responsible for but little additional expense and consequently was rather profitable.

Bad debt losses were charged where they occurred. These were relatively high for all departments except Dept. A, which lost very little.

Delivery expense covers the cost of operating the delivery trucks and the wages of the delivery man. The amount is distributed according to the actual time the trucks were used in making deliveries for the various departments.

Occupancy expense for this store amounted to $4,000 and was divided on the basis of space occupied. Occupancy includes the rent of the building and the cost of heat, light, and other services such as repairs, necessary to keep it in usable condition. When a building is owned, the taxes, depreciation, repairs, and insurance are included as occupancy cost. The space is allotted to the different departments on the basis of use.

The building has 6,000 square feet and the occupancy cost is $4,000, or 66⅔¢ per square foot. The allocation is made as follows:

Dept. A...........3075 sq. ft. x 66⅔¢	$2,050
Dept. B............615 sq. ft. x 66⅔¢	410
Dept. C............114 sq. ft. x 66⅔¢	76
Dept. D...........1155 sq. ft. x 66⅔¢	770
Dept. E...........1041 sq. ft. x 66⅔¢	694
	$4,000

Occupancy expense is commonly distributed to various lines or departments on the basis of the amount and location of space. When a store has two sales floors, it is customary to allocate 65 per cent of the rent to the first floor and 35 per cent to the basement or the second floor. With three floors, it is

customary to allocate one-half the rent to the first floor, one-fourth to the basement and one-fourth to the second floor.

In a first floor room that is 100 feet deep, the value of the space is often divided: 25 per cent to the front 10 feet; 25 per cent to the next 20 feet; 25 per cent to the next 30 feet; and 25 per cent to the rear 40 feet. If a room is 50 x 100 feet and rents for $3,000 a year or 60 cents per square foot, the front 10 feet would be assigned $750 or $1.50 a square foot; the next 20 feet $750, or 75¢ a square foot; the next 30 feet, $750, or 50 cents per square foot; and the rear 40 feet, $750, or 37½ cents per square foot.

Insurance on stock is divided on the basis of average inventory as shown in the following example:

	INVENTORY		INSURANCE	
	Amount	Per cent	Per cent	Amount
Total	$25,000	100	100	$300
Dept. A	7,500	30	30	90
Dept. B	4,000	16	16	48
Dept. C	2,000	8	8	24
Dept. D	9,000	36	36	108
Dept. E	2,500	10	10	30

Insurance on equipment and supplies covers the counters, display cases, tables, racks, chairs, cash registers, and other equipment and fixtures. This insurance is allocated on the basis of the value of the equipment used in each department.

Liability insurance includes public, employer's, automobile, and contractor's liability. It is divided among the departments on the basis of the number of people employed in each department. One-eighth of this insurance is charged to Dept. D; three-eighths to Dept. E; three-eighths to Dept. A; and one-eighth is divided between Depts. B and C.

Taxes on inventories, equipment, and supplies are divided on the basis of investment as shown in the following example:

	INVESTMENT		TAXES	
	Dollars	Per cent	Per cent	Dollars
Total	$35,000	100.0	100.0	$350
Dept. A	10,000	28.6	28.6	100
Dept. B	4,000	11.4	11.4	40
Dept. C	2,000	5.7	5.7	20
Dept. D	9,000	25.7	25.7	90
Dept. E	10,000	28.6	28.6	100

Interest covers the cost of the investment in inventories and equipment and is distributed on the same basis as taxes.

Miscellaneous expenses are divided among departments on the basis of sales as shown below:

	SALES		MISCELLANEOUS EXPENSES	
	Dollars	Per cent	Per cent	Dollars
Total	$175,000	100.0	100.0	$1,200
Dept. A	110,000	62.9	62.9	754
Dept. B	12,000	6.8	6.8	84
Dept. C	10,000	5.8	5.8	68
Dept. D	25,000	14.2	14.2	170
Dept. E	18,000	10.3	10.3	124

Summary of expense allocation. Salaries and wages, traveling expenses, advertising, bad debt losses, and delivery expenses were distributed among the five departments on the basis of records and estimates. Occupancy was distributed on the basis of floor space occupied. Insurance was allocated on the basis of the risk insured. Taxes and interest were divided on the basis of investment in stocks and in equipment. Miscellaneous expenses were distributed on the basis of sales. It is customary to use sales as a basis of distribution for those expenses for which no better or more logical basis is known.

After the expenses are distributed they are totaled by departments and subtracted from gross margins for the departments. This shows a profit of $2,665 for Dept. A, $215 for Dept. B, $3,175 for Dept. D, $4,892 for Dept. E. The total profit from the profitable departments was $10,947. Department C shows a loss of $1,382. Subtracting this loss from the profits made in the other departments leaves a net profit of $9,565.

Analysis. This retailer had thought Dept. C was profitable and had been promoting it. Now he discovers that the department produces only a small margin and has fairly high expenses. The latter are caused by the relatively large amount of time devoted to the sale of this merchandise. The retailer may seriously consider discontinuing Dept. C. Other factors, however, may justify continuation of the Department for a while, at least.

He may not need Dept. C's space (114 square feet) for other purposes and believe that if Dept. C were discontinued there would be a temptation to increase the stocks and slow up the

turnover of the other departments. He may reason that other similar stores usually have a department such as Dept. C and that he cannot afford to discontinue it. The bad debt loss indicates either that sales are made to poor credit risks or that collections are not pushed, or perhaps both are true. Also advertising expense is relatively higher for Dept. C than for other departments. If Dept. C is a new department which has not yet been fully established, it perhaps should be continued.

In summary, this retailer considers from the expense standpoint what operating expenses might be eliminated by discontinuing a line or department and what expenses would not be reduced. The saving in expenses may then be compared with the gross margin made on the line to see if it is meeting the "out-of-pocket" or variable expenses. He also considers the contribution to income, both gross and net, which might be made by the addition of other new lines. This alternative may be attractive. However, the line to be dropped contributed something to margin, and perhaps no substitute will do as well. Finally he may consider future possibilities. Today's undesirable line may be tomorrow's profitable line.

The total business is profitable, due largely to the operations of Dept. E, which produced more than one-half of the total profit. The merchandise sold in this department has the highest rate of gross margin. A great deal was spent in advertising the department but the results justify the expenditure. Serious consideration should be given to expanding the department.

Profit by brands. A retailer often wishes to know which manufacturer's line is most profitable. He may have a choice of brands or lines of several manufacturers or wholesalers. Some of these carry higher markups than others. Manufacturers with brands carrying low markups may point out that their products have created so much consumer demand that the retailer needs to expend little selling effort and that his selling expenses are therefore low. On the other side, the seller whose product carries a higher markup may point out that it is the retailer who really creates demand, that consumers buy the goods which retailers recommend, and that if a retailer will push a line he can create wide acceptance in his community

regardless of national advertising. What is the truth of these arguments?

Some indication of the relative profitableness of brands and lines can be obtained by determining the total gross margin earned by each. The expense allocation method just described can be used in analyzing the lines of various manufacturers, provided that the retailer has a record of the salesmen's time spent in selling the different lines. In a small, non-departmentalized store where the salesmen sell all lines, this analysis is difficult. Though not impossible, it is expensive for such a store to keep the necessary records or to make the required time studies. If the articles are large, however, it may be possible for the salesmen to keep account of the time during selected test periods.

Questions

1. Why should records be kept? What did the study made by the Department of Commerce reveal in this connection?
2. What are the benefits of keeping sales records?
3. How may a record of sales by lines or departments be kept?
4. What methods may be used to keep records of sales on credit?
5. What is an invoice register? What information is kept in it?
6. What methods may a retailer use in safeguarding his cash?
7. What are the benefits of departmental accounting?
8. In departmental accounting is there an ideal basis on which to allocate each expense? Indicate different bases on which it may be possible to distribute various expenses.
9. George Young operates a variety store. Last night he had cash on hand of $47.61. He paid out $8.39 today. His cash register shows that he received $165.83 today; actual cash on hand is $204.00. Prepare a proof of cash for Mr. Young.
10. R. P. Wallen operates a shoe store. On December 31 he owes his bank $560, and merchandise creditors $110. Cash in his safe and in his bank account amounts to $1,650. Customers owe him $335 and the value of his merchandise is $8,700. His sales for the year are $22,000 and at the end of the year his merchandise on hand amounts to $9,000. He paid himself a salary of $2,400 and a salesman $1,500. His occupancy expense was $1,320; advertising, $400; bad debt loss, $200; and all other expenses, $880.

Prepare a profit-and-loss statement and a balance sheet for Mr. Wallen.

11. Smith Saunders operates a general store which he has divided into three departments. The dry goods department is the largest and the grocery the smallest; the hardware department is somewhat larger than the grocery department but much smaller than the dry goods department.

The following information is for a recent year:

	DRY GOODS	GROCERIES	HARDWARE	TOTAL
Sales	$50,000	$20,000	$30,000	$100,000
Inventory January 1	20,000	10,000	15,000	45,000
Purchases during the year	25,000	8,000	16,000	49,000
Inventory December 31	15,000	9,000	11,000	35,000
Owner's salary				5,100
Salesmen's salaries				7,500
Office salaries				3,600
Advertising				3,000
Losses on bad debts				500
Delivery expense				2,400
Occupancy				5,000
Insurance on stock				500
Insurance on equipment				300
Insurance, other				200
Taxes				270
Interest				1,200
Miscellaneous expense				3,830

Determine the profit for each department. Distribute expenses as follows:

EXPENSE	BASIS
Owner's salary	Equally
Salesmen's salaries	Sales of department
Office salaries	Equally
Advertising	Sales
Loss on bad debts	Credit sales
	dry goods, $25,000
	groceries, $5,000
	hardware, $20,000
Delivery expense	Delivered sales
	dry goods, $10,000
	groceries, $5,000
	hardware, $15,000
Occupancy expense	Space occupied
	dry goods, 6,000 sq. ft.
	groceries, 1,000 sq. ft.
	hardware, 3,000 sq. ft.
Insurance on stock	Average inventory

EXPENSE	BASIS
Insurance on equipment	Investment dry goods, $20,000 groceries, $2,500 hardware, $7,500
Insurance, other	Number of employees dry goods, 2 groceries, 1 hardware, 2
Taxes	Investment
Interest	Investment
Miscellaneous expenses	Sales

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Tax Records and Reports

It is necessary for the retailer to keep certain records and make certain reports in order to comply with tax laws and regulations. He must keep records in connection with Federal income, social security, withholding, and, in a number of States, sales taxes.

No attempt is made here to give advice on the complex tax laws and regulations, or on the different state tax laws. Minor changes in the tax laws are being made continually, and these may change the records and reports required. However, it is not likely that the general nature of the reporting requirements will be fundamentally changed in the near future. Many retailers prefer to employ an accountant or attorney to assist them in the preparation of their reports. Because of their greater familiarity with the details of such matters, these men may be able to save a retailer more than the fee which they charge. Even though a retailer does not make his own return he should be familiar with the tax requirements and records.

Federal Income Taxes

Although it is impossible to discuss the many complex problems or unusual situations which may arise in connection with the preparation of a Federal income-tax return, the retailer who keeps adequate records will find it a relatively simple matter to prepare his income-tax statement. Most of the necessary data, insofar as the business is concerned, can be obtained from the

annual profit-and-loss statement. Retailers who operate their stores as individual proprietorships will use Form 1040. If the store is operated as a partnership, the income-tax return for the business will be filed on Form 1065; and if the store is incorporated, the return will be filed on Form 1120.

Employment (Social Security) Taxes

The provisions of the Social Security Act include two insurance programs: (1) Old-age and survivor's insurance and (2) unemployment compensation. The old-age and survivor's insurance system is administered entirely by the Federal Government through the Social Security Board of the Federal Security Agency. For unemployment compensation, the Social Security Act established a coöperative Federal-State system.

Old-age and survivor's insurance. This insurance program applies to employers of one or more employees. Thus, if a retailer has one employee, he must keep certain records to enable him to make accurate reports which are required under this law.

The Social Security Board, in conjunction with the Bureau of Internal Revenue, has issued an outline of the employers' duties under the Social Security Act, from which the following is quoted:

> Keep a record of the social security account number of each of your employees. Enter the number on your permanent records.
>
> Keep accurate payroll records showing the name, address, and social security account number of each employee, the amount paid to him, and the amount of employee's tax deducted from his wages. No particular form is prescribed for keeping these records.

The Social Security Board's outline contains a further statement:

> Not later than the last day of April, July, October, and January of each year, file with your local Collector of Internal Revenue your return on Form SS-1a. . . . You must include in your tax return on Form SS-1a, a report of the name and social security account number of each employee, and the amount of taxable wages paid the employee.

Form SS-1a has a statement about the records which the retailer must keep:

Each employer must keep sufficient records to enable him to fill in the return accurately for each employee, and to enable the collector to verify the amount of taxes due. Such records must be retained for a period of four years from the date when the taxes were paid, and must at all times be open for inspection by Internal Revenue officers.

The employer has a further responsibility:

You are required to furnish each of your employees a statement in a form suitable for retention by the employee showing the taxable wages paid to the employee . . . and the amount of employee's tax with respect to such wages . . . (The employer is also required to furnish a similar statement in connection with withholding taxes, which are discussed below.)

Unemployment compensation. Both a Federal tax and contributions under State laws are levied under the unemployment compensation program. An employer is not obligated to pay the Unemployment Tax unless— ". . . you have eight or more employees on a total of 20 or more days during the calendar year, each such day being in a different calendar week. . . ." Retailers having eight or more employees for the requisite period of time must file an annual tax return under the Federal unemployment compensation system.

Although the retailer may never have as many as eight employees and thus may not need to file a Federal return, he may be subject to his State Unemployment Compensation Law. In some States, the unemployment compensation law applies even if the retailer has only one employee. Each State administers its own unemployment compensation law, and since the required reports are different in each State, they are not described here. In all events, however, the retailer should inquire from his State Unemployment Compensation Board just what his obligations are in this respect.

Withholding taxes. Every employer must deduct and withhold specified amounts from the wages of his employees for Federal income taxes. That is, the employer acts as an agent

of the government in collecting income taxes by deducting the amount of the tax from the wages of his employees.

The amount of tax to be withheld from the wages of each employee depends on the amount of his earnings, on whether the employee is married, single, or the head of a family, and also on the number of his dependents. Further, the amount of the withholding tax is subject to change each year as the income-tax rates change. Consequently, the method of computing the amount of tax to be deducted and withheld from employees' wages will not be discussed here.

Records. Every employee is required to furnish his employer with a signed withholding-exemption certificate, which contains the necessary information so that the employer can compute the employee's exemption and the amount of the withholding tax. On this certificate, the employee states whether he is married, single, or the head of a family, and the number of his dependents. If the employee is married, he must also state whether he claims all, none, or half of the withholding exemption allowable to married persons. If there is a change in the employee's status in regard to his withholding exemption, he is required to furnish a new certificate to his employer not later than ten days after such change occurs.

In general, the type of records needed in connection with the withholding tax are the same as those required for the old-age and survivor's insurance program under the Social Security Act, which were described above. In fact, the individual employee's compensation record which is used for recording the deductions and other data required for Social Security taxes can also be used for recording withholding taxes merely by including another column.

Reports. In addition to keeping the above records, all employers who withhold taxes from their employees' wages are required to file three different reports with the Collector of Internal Revenue. These are as follows:

1. Quarterly Return of Income Tax Withheld on Wages.
2. Statement of Income Tax Withheld on Wages (Employee's Receipt).

3. Reconciliation of Quarterly Return of Income Tax withheld (Form W-1) with statements of Income Tax withheld (Form W-2).

Every employer who is required to withhold a tax on wages must file a quarterly return. Also, the employer must pay the tax to the Bureau of Internal Revenue on or before the last day of the month following the close of each quarter of each calendar year.

In addition to the quarterly return, every employer is required to furnish each employee with an annual statement showing the wages paid and the amount of tax withheld during the calendar year. This statement should be given to the employees by January 31 of the year; or, if the employment ends before the close of the year, within thirty days after the last payment of wages is made. In the case of intermittent employment, if it is not expected that the employee will be re-employed, then a statement of the amount withheld must be furnished him at the end of any term of employment. If there is a reasonable expectation on the part of both the employer and the employee of further employment, then the statement does not need to be furnished the employee immediately.

Employers must send to the Collector of Internal Revenue a duplicate of each statement furnished to employees when they file their final quarterly return for the fourth quarter of the calendar year. If the employer discontinues business or ceases to be an employer, he should file duplicates of all statements with his final return, in whichever quarter it is made.

The quarterly return for the fourth quarter of the year must also be accompanied by a reconciliation. That is, the total tax withheld as shown by the sum of the amounts on the four quarterly returns must agree with the total as shown by the sum of the taxes withheld from individual employees. Employers should also send a list, such as an adding machine tape or some other convenient proof, showing the amounts of tax withheld from each employee.

Payment of tax. Every employer required to withhold income taxes from wages is liable for the payment of the tax required to be withheld. The tax withheld by the employer

is a special fund in trust for the United States Government. If possible, retailers should deposit withheld taxes in a separate bank account, or otherwise physically segregate such cash. Any errors made by employers, either in the withholding or payment of the tax, for any quarter of the calendar year, may be corrected in any subsequent quarter of the same year.

Sales Taxes

Retail sales taxes are in effect at present in twenty-three states, but the exact nature of the taxes, the tax rate, and other important details vary in the several states. Consequently, it is not feasible to describe the specific sales-tax records used by retailers in all these states. The retailer should acquaint himself with the law and adapt his record-keeping to the requirements in his State.

We can, however, discuss in general the records which must be kept for sales-tax purposes. These are of two main kinds: First, a record of the amount of sales or gross receipts subject to tax and the amount of sales or gross receipts exempt from tax; secondly, the amount of taxes to be paid. Where the law provides that general sales taxes either may or must be collected from customers, the amount actually collected also should be recorded.

Exemptions and deductions. In practically all states that levy retail sales taxes, sales of certain kinds of merchandise or sales to certain classes of customers are exempt from the general sales tax. For example, sales of motor fuel, cigars, cigarettes and tobacco, beer, seeds, and feeds are exempt from the general sales tax in several states because specific taxes have already been levied on them and paid by the wholesaler or the manufacturer.

1. Merchandise sales exempt from retail sales tax. When a retailer handles both taxable and non-taxable merchandise, he is faced with the problem of recording the two types of sales separately.

When the nature of the goods exempt from the general sales tax is such that they can be assembled in a single selling department, a departmental sales record will provide the necessary

information. For such merchandise, one of five methods of recording departmental sales can be used: (1) the use of a sheet kept beside the cash register; (2) departmental totals in cash registers; (3) departmental symbols on cash-register tape; (4) separate departmental cash registers, and (5) perforated departmental tickets.

The nature of the merchandise exempt from retail sales taxes is often such that it can not as a practical matter, be assembled in separate departments. The amount of sales of a tax-exempt item often can be estimated by studying the inventory and purchase data and calculating the quantity sold. The quantity sold may be multiplied by the average or typical retail selling price, to find the sales of the item. For example:

	No. of items, packages, etc.
Beginning inventory (actual count)	50
Plus: Quantity purchased (from invoice)	300
Total	350
Less: Ending inventory (actual count)	45
Quantity sold (packages)	305
Sales during period, 305 × 10¢ (10¢, retail selling price)	$30.50

Of course, if the price of such items changes frequently, this method would not yield accurate results unless it were possible to adjust the average retail selling price to reflect price changes.

The sales of such items also can be estimated from inventory and purchase data by adding an average markup or "mark-on" to the cost of goods sold. This method is illustrated in the following example:

Beginning inventory at cost (actual count)	$15.25
Plus: Purchases at cost (from invoices)	50.65
Total	65.90
Less: Ending inventory at cost (actual count)	10.50
Cost of goods sold	55.40
Plus: Markup on cost of 33⅓% (⅓ of $55.40)	18.47
Estimated sales	$73.87

Before a retailer uses these methods of estimating the sales of items exempt from the sales tax, he should make certain that the laws and regulations in his State permit their use.

2. Sales of goods exempted from tax because of their uses. A number of states exempt from general sales taxes any sales of goods that are to be used by certain buyers, or for certain specified purposes. For example, sales to the Federal Government, as well as to the states and political subdivisions, may be exempt. Since most governmental units require the seller to furnish a written invoice of some kind, the retailer needs only to keep copies of these invoices, or signed receipts of sales to government agencies. Such sales can be deducted from total receipts in reporting the sales subject to tax. Some states also exempt sales to charitable institutions, state-supported public schools, hospitals, and so on. These sales can be handled in a manner similar to sales to governmental units.

Sales by retailers, at wholesale, to other retailers are exempt from the general retail sales tax in a number of states. This is important to many retailers who do both a wholesale and retail business. Some states have devised certificates which the purchasing retailer signs and the selling retailer remits to the tax administrator as proof of such exempt sales.

The most troublesome problems arise when the exemption for use applies to a commodity which is sold frequently and in small amounts. For example, in some states builders' supplies sold to contractors are exempt from the general sales tax but the same supplies are taxable when sold to the household consumer.

The sales-tax administrators of some states expect stores in the same kinds of business to remit taxes on comparable parts of their total retail sales. A retailer who has a larger than average proportion of his total sales in tax-exempt business may be called upon to furnish proof of the amount of his exempt sales. The adequacy of his sales records on tax-exempt merchandise is the only defense the retailer has against any assessments which might be made against him for additional tax.

3. Deductions for cash discounts and returned goods. Most of the states allow deductions for cash discounts given to cus-

tomers, and for refunds on returned goods. In other words, where the law permits, the retailer reports net sales instead of gross sales, as a basis for computing the general sales tax. Gross sales minus returns, allowances, and discounts, gives net sales, the amount on which the retailer pays a tax when it applies to net sales.

4. Deductions for bad debts. Deductions for bad debts apply only in those states where the general sales-tax law requires the retailers to pay the tax on credit sales on the full amount of the sale regardless of the amount collected. Some states allow as a deduction from gross sales, or gross receipts, the amount of bad debts charged off for income-tax purposes on which the sales tax has already been paid. Other states allow the amount of sales tax paid on the bad debts to be deducted from taxes due. Although the method of allowing the deduction varies, the result is the same. The retailer, if he wishes to claim a deduction, must keep a record of the amount of bad debts charged off to loss.

Charge sales. Some states require the tax on credit sales to be paid on the total selling price at the time the sale is made, regardless of when the cash is actually collected. In these states the tax must be included in the tax return for the period immediately following the date of the sale. Other states either require or allow the tax to be paid on the cash collections on credit sales made during a preceding tax period. Still other states allow the tax to be paid either on the total selling price, and included in the tax return immediately following the date of sale, or on collections received during the preceding tax period, at the option of the retailer.

1. Tax based on total selling price. In those states where the dealer is either required or allowed to pay the tax on the total selling price and where the tax is a stated percentage of sales or gross receipts (see discussion below), charge sales do not create any additional problem of record-keeping.

In states where the tax on credit sales to be paid by the retailer is the actual amount of tax collected from customers (see discussion below), additional records for determining the tax are necessary. Even in these states, however, the columns

in a sales record are sufficient to record the amount of credit sales subject to tax.

2. Tax based on current collections. In states where there is a tax on current collections received on all types of credit sales instead of on the total selling price of these credit sales, a different procedure is necessary. In this case the retailer pays a tax on cash sales plus collections, and reports this amount instead of total sales.

In some states the retailer is required to report cash sales and collections separately. These amounts may be determined either daily or monthly from the regular records.

Recording the amount of the tax. The method of calculating the amount of State tax depends, of course, on the kind of sales-tax law in effect. These tax laws fall into two general groups: (1) Those in which the tax is to be paid by the retailer and is a stated percentage of his total sales or gross receipts, and (2) those in which the retailer acts as an agent of his state in collecting the tax. In the second case the retailer is required to remit to the state the actual amount of tax collected from customers but not less than the amount due under the legal rate. He must keep a record of the actual amount of tax collected from customers, as well as the amount of sales subject to tax.

1. Where tax is percentage of retailer's sales or gross receipts. Under the first group of laws, the amount of tax collected from customers is not necessarily the same as the amount of tax which the retailer has to pay the state. In practice, he may collect as sales taxes amounts above or below the amounts which he must remit to the State collector.

Records may be kept in either of two ways: (1) The dealer may keep a record of his gross receipts, that is, sales, plus tax collected; or (2) he may keep a record of merchandise sales exclusive of tax, and a separate record of sales taxes collected from customers. Under the first method, the state sales tax can be determined by multiplying the gross receipts by the tax rate. The procedure, however, results in an indicated tax that is slightly higher than the amount which the retailer needs to pay to the state. This is because he would be paying a sales tax

on the amounts he collected from customers as sales taxes. For example, assuming the tax rate is 2 per cent, then the tax which the dealer pays under the first method, as compared to the second method, is as follows:

1. Sales and sales tax recorded together:	
Gross receipts (sales plus tax)	$2,040.00
Sales tax paid by retailer (2% of $2,040.00)	40.80
2. Sales and sales tax recorded separately:	
Sales (exclusive of tax)	2,000.00
Sales tax collected	40.00
Gross receipts	2,040.00
Sales tax paid by retailer (2% of $2,000)	40.00

Under the first method he pays a tax of $40.80, as against a tax of $40.00 under the second method. It should be noted, however, that in some states, for example, Indiana, the laws specify that any sales tax collected from customers must be considered as gross income and is itself subject to sales tax.

Since it is much simpler to keep a record of gross receipts than it is to record sales and sales taxes separately, the retailer may prefer to use this method if he can do so without paying a higher tax. It is possible to use the gross-receipts figure and yet, by a simple calculation, get the same results as when sales taxes are recorded separately. For example, assume the tax rate is 2 per cent:

1. Gross receipts (sales plus tax)	$2,040
2. Sales (gross receipts of $2,040 divided by 1.02)	2,000
3. Sales tax paid by retailer (gross receipts minus sales or 1 – 2)	$ 40

If the tax rate were 3 per cent, the gross receipts would be divided by 1.03, and so on.

2. Where tax is amount collected from customers. In those states where the retailer must remit to the state the actual amount of tax collected from customers, it is necessary to keep a separate record of the amount of tax collected. There are several ways of determining the amount of tax collected. Perhaps the simplest way is to segregate such cash. The retailer can have a section in his cash drawer, or a tax box, into which he drops the actual cash collected for sales tax on each cash sale.

At the end of the period specified by the law, the amount collected as tax can be entered in a column headed "sales tax."

Two other methods can be used for determining the amount of sales tax collected. Some cash registers have a sales-tax key on which the amount of tax collected on each transaction can be rung up. The register accumulates the total amount of tax collected. Another method is to have a small manually-operated counter attached to the register, which records the tax collected on each transaction and accumulates a total. At the end of the period the totals can be entered in the records. Under these two methods it is not necessary actually to segregate the cash received from sales taxes.

The sales slip can be used for recording the sales tax on credit sales. In those States where the tax on credit sales is based on total selling price, the tax can be entered on the sales slip and included in the total charge at the time the sale is made and then entered in the sales-tax column of the sales record. In those states where the tax is based on current collections, the tax can also be entered on the sales slip at the time the sale is made. This sales-slip system can also be used in those states where tokens are used.

Use of tokens. In states where tokens are used, the most practical way to determine the amount of tax collected is to have a "tax box" into which the cash received as tax, cash from the sale of tokens, and the tokens collected from customers are deposited. (The amount of tax collected on charge sales can be recorded on sales slips as described above.) The amount in the box is also counted at the end of each day or week, and is entered in the sales-tax column.

For example:

Amount in tax box at end of period		
Cash	$20.00	
Tokens	0.157	
Total		$20.157
Less: Amount in tax box at beginning of period:		
Cash	$ 1.00	
Tokens	0.251	
Total		$ 1.251
Amount of tax collected which is to be paid to State		$18.906

Conclusions. In the preparation of the tax reports required in connection with Federal and State income taxes, withholding taxes, social security taxes, and general sales taxes, it is necessary for the retailer to have adequate and accurate records. This imposes a burden of record-keeping from which the retailer cannot escape. The basic data necessary to prepare the tax reports will be available if he has an adequate set of records. The object of record-keeping, however, is not merely to provide data for tax reports. Rather, the fundamental objective is to provide facts that will guide the dealer in the successful and profitable management of his store.

Questions

1. Obtain a copy of the current income tax form which retailers use and fill it in for the retailer mentioned in question 11 at the end of Chapter 28.
2. For what does the Social Security Act provide?
3. What are an employer's duties under the Social Security Act?
4. What reports must the employer make? What records must he keep?
5. Are all employers required to pay a Federal unemployment tax?
6. Are all employers required to deduct certain amounts from wages?
7. What withholding tax information is the employee required to furnish his employer?
8. What reports is the employer required to file with the Collector of Internal Revenue?
9. When a retailer handles merchandise subject to a sales tax and merchandise exempt from it in the same store, how can he determine the amount of the tax he must pay?
10. Where sales are tax-exempt because of the use to which the goods are to be put, what records should be kept?
11. Under what circumstances can bad debts be deducted from sales in arriving at the amount of sales tax that is due?
12. On the basis of the method of calculating the sales tax, how may sales-tax laws be classified?
13. Where the sales tax is a percentage of the retailer's sales or gross receipts, what records should the retailer keep?
14. If sales are multiplied by the tax rate, will the correct tax be paid?
15. Where the retailer must remit to the state the actual amount of the tax collected, how may he keep a record of the amount of the tax?

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Stock Control and Stock Turnover

The proper control of stock is a fundamental of good retail management. Stock must be on hand in the proper quantity and it must be sold within the proper time. The quantities of the various kinds of merchandise which compose the inventory must be maintained in the proper proportion to each other. Some of the various kinds of merchandise will sell at a faster rate than do others.

The benefits of stock control are increased customer satisfaction, an increased rate of stock turnover, decreased markdowns, and more efficient buying. If the rate of stock turnover is increased, and other conditions remain constant, expenses are reduced and profits are increased. The following expenses are reduced: interest, insurance, taxes, rent, heat, light, and usually, the salaries of salesmen.

Stock control reduces the amount of dead stock, or number of "sleepers." Articles left in stock too long may become soiled, dirty, broken, or obsolete and need to be marked down and sold at a loss. The capital released from dead items, shelf warmers, or sleepers can be invested in salable merchandise which will increase the store's profit. Preventing the accumulation of dead and slow-moving items and putting the capital into good stock will increase sales and profits.

Stock control is the basis of good buying. A stock control system informs the retailer when his stock of an item is low and more should be ordered. Stock records also show seasonal sales and indicate when, as well as how many, articles should be

bought of goods with seasonal demand. Stock records can be used to show the volume of sales and the changes in demand for merchandise. They show which goods should be bought in larger quantities, and which should be bought in smaller quantities, or discontinued.

Methods of Stock Control

There are three general methods of controlling stock: by inspecting the stock; by taking frequent physical inventories; and by keeping a continuous record of all stock sold and received, that is, a perpetual inventory.

Inspection system. Under the inspection system, the retailer checks over his stock from time to time and notes the items which are low and need replenishing. This system is only as good as the men who do the inspecting. Some stores which claim to use this system really have no stock control system at all. Stock is inspected infrequently and hastily. Too often an out-of-stock item is not reordered until a customer asks for it. Then it is entered on the want list and is bought from the next salesmen who visits the store. Some retailers permit the wholesaler's salesmen to inspect the stock and tell them what items should be bought. Salesmen may do a good job but all too often they simply check the items they are interested in; or they may inspect only enough stock to make up a fair-sized order and go to the next store. Without disparaging their assistance in any way, an efficient retailer naturally prefers to do his own inspecting as he knows his customers' needs much better than the salesman.

A retailer who knows his stock intimately, who knows local demand, and who inspects his stock frequently and carefully can do a pretty fair job of stock control. To do a good job, the retailer needs model stock figures and a good method of stock arrangement. Often he uses special devices such as labels for danger signals on minimum quantities.

Space assigned to each article. To make the inspection successful it is desirable to assign a definite space to each item. If the space is partly empty, the retailer's attention is attracted to

it and he can determine from the number on hand how many are needed to bring the stock up to normal. For example, a compartment on a table may hold twelve of an item. If the space is not full, the retailer looks for reserve stock under the table. Perhaps the salesclerk neglected to fill the display space. If this is the case, the display is filled and the omission is called to the clerk's attention. If, however, there is none of this particular item in reserve, it is entered on the want list. Perhaps the normal order is two boxes, and the minimum quantity to be kept in stock is twelve.

Label minimum quantity. When the salesman emptied the last box the items should have been entered on the order list. The twelve units on the display table constitute the minimum quantity that must be carried in stock. When the last one was taken from the last box an entry should have been made on the order list. To reduce the number of such omissions, tags may be placed in the bottom boxes. When the last box is emptied, the tag is dropped in a special receptacle. These tags are collected daily and furnish the basis of reorders. If one case of an article is the minimum quantity, this case is labelled, perhaps with a red tag. When it is opened the red tag is put in the order receptacle. Perhaps one-half or one-fourth of a case is the minimum quantity which should be in stock. When the goods are received, one case is opened, and only the minimum quantity left in it. The case is then closed and placed on the bottom of the pile or shelf with the red tag fastened to the top of the box, or left on top of the goods inside. When the box is opened to make a sale or place the goods on display, the tag is sent to the buyer.

Labeling the minimum quantity may be impractical when all goods are on display. Here the retailer must note that a given shelf, compartment, rack, or hook is not full. The minimum quantity, together with the manufacturer's number, price and so forth may be noted on the shelf, or it may be kept in the stock book.

Repair parts are often kept in compartments of sloping racks some seven feet high and records are made on a card index. When a request comes in for a particular part, the salesman

uses the index to determine in which rack and compartment the item is kept. When he obtains the part, he notes the quantity in stock and if it is low he makes a note for a reorder.

A visual aid that may be satisfactory for articles kept in drawers is a small flag fastened on the inside of the drawer. The salesman waiting on a customer notes that the stock of some item is low, but he does not wish to delay the customer by taking time to write down the name and size of the item. As he closes the drawer, he lifts the flag. When there are no customers in the store, records are made of the flagged items. A weakness of this system is that the same articles may be signalled several times before the reorder is received. To prevent duplicate reorders, recent purchases should be checked before another reorder is given.

With a good arrangement of stock and with model stock figures, the inspection system will reduce the amount of out-of-stock merchandise as well as prevent stocking too much of an item. With good judgment on the part of the buyer, an average or higher rate of stock turnover may be secured. This system requires close attention to detail to obtain satisfactory results, but it requires less clerical work than the two systems described below. The inspection system does not give sales information for individual items. The data must be obtained from an analysis of invoices and inventories. If an inventory is taken only once a year, it is very hard to determine seasonal sales. Here again, the retailer must depend on his judgment. In a small store the retailer may have a fair knowledge of how various articles sell in various months. When the facts are obtained, however, it is found that few dealers have accurate information.

Frequent physical inventories. Although most small stores use the inspection system, this system alone is seldom satisfactory for larger stores. Owing to the expenses of a perpetual inventory system, relatively few stores use it in all departments. Thus the tickler system of taking frequent physical inventories is the one used by many of the better stores, especially those of moderate size, and by many chain stores. If followed carefully, it will limit the number of out-of-stock articles. If, however, a

particular article is selling faster than usual and faster than expected, this system will not detect the shortage until the next inventory is taken. Of course, if the stock is low or exhausted, a salesman will probably note it on the want list. When this system is used, however, salesmen probably are not trained to be as alert for shortages as when stock is controlled by inspection.

Frequent physical inventories help the retailer to guard against overstocks. The number on hand at the first of the month, plus the number purchased during the month, minus the number on hand at the end of the month equals sales. For example: ten units are on hand on January 1, six are purchased during the month, and fourteen are on hand at the end of the month. Therefore, two have been sold during the month. Sales of individual articles may be computed in this way for monthly inventory periods. The retailer also must keep his invoices that have been checked against receipts to show what quantities were received during the month.

The check list is another device used in taking a physical inventory. The check list, however, has room for only one inventory whereas a stock record has space for several—perhaps twelve, fifteen, or more. If a permanent record of inventories and sales is desired, the information must be transferred from the check list to the stock record.

Perpetual inventory. A perpetual inventory system may keep records of individual items or units; or it may be used to keep records of the dollar values of goods in various departments, lines, or classifications; or it may be used to keep a record of both units and dollar values.

With a perpetual inventory system, the retailer can determine from his stock records at any time the quantity of each article in stock. The quantities of all goods received are added to the quantity on hand, and the sales deducted from this figure. Thus, the store has a constant record of the quantity of an item on hand and on order.

The stock record is usually kept on specially ruled cards or in forms kept in a loose-leaf binder. One card or one page may be devoted to each article. This card has spaces for the name

FORM FOR PERPETUAL INVENTORY

ARTICLE.................... SIZE OR COLOR.............. UNIT.............. STOCK NO...............

MIN. STOCK......................... QUANTITY TO ORDER................ VENDOR...............

Month	Order or Invoice Record	Days	1	2	3	4	5	6	7	8	9	10	to 31
		On Hand											
		Rec'd											
		Sold											
		On Order											
		On Hand											
		Rec'd											
		Sold											
		On Order											

The form is wide enough to record the transactions for a month, and may be long enough to hold twelve months, or a six months' record may be kept on each side. Forms may be kept in a loose-leaf binder.

of the article, its stock number, its cost, selling price, source (manufacturer or wholesaler), size or color, and the quantity to be ordered at one time. It has spaces for each day of the month for the number of units on hand, number received, number sold, and perhaps the number on order. If the quantity of an item on hand is 2, the number received 3, and the number sold 1, the balance carried forward to the next day is 4. Each side may have space for six months, so that one sheet or card keeps the record of one item for a year. When the quantity in stock reaches the minimum specified, an order is made out by the stock clerk and given to the buyer, who places the order. Barring unusual sales, or delays in the receipt of goods, this system should prevent the store ever being out-of-stock on any regularly-stocked article.

Information as to the sales, receipts of goods, and orders should be sent to the stock clerk daily. The principal difficulty and expense occur in keeping accurate, itemized records of sales. This may be done by attaching perforated sales tags to each article. When an article is sold, half the tag is dropped in a box for the stock clerk. Another method is to require salesmen to make out sales slips for all articles sold, giving the

stock number, size, and price of each. Carbons of the sales slips then are sent to the stock clerk. Owing to haste or poor training, salesmen often make errors that are transferred to the stock records. Errors also result when returned goods are placed in stock without advising the stock clerk. Stolen goods or other stock shortages may cause trouble. It is necessary to check the stock records against physical inventories from time to time in order to correct the stock records.

Short cuts may be devised to save work. A perpetual inventory system is expensive for small items, unless the unit of stock is made much larger than a single item. By making the stock unit a hundred, a gross, or a thousand, the amount of record-keeping is considerably reduced.

The records may be kept in dollars rather than physical units. The merchandise is entered on the records at selling price. It is classified and controlled by groups. Each group is assigned a number or letter and a stock sheet is made up for each group. All purchases of a particular class of merchandise are entered on the record at selling price. When any particular kind of merchandise is received it is charged to the group. When it is sold, it is credited to the group. From the record it is easy to derive the value of the goods in stock.

To obtain sales data, each salesman records the sales by groups. A sheet with a separate column for each group may be placed beside the cash register. Sales are entered in the proper columns. At the end of the day, the columns are totaled to obtain the total sales for the day in the various lines. If a large cash register is used, it may have keys enough for each department in the store. In this case total sales by lines can be recorded on the cash register. Dollar control is an excellent method of keeping the stock properly balanced between departments.

Dollar control does not give the number of individual items in stock. Thus the record may show that the store has $300 worth of a particular line of merchandise on hand on March 15, and this may be the correct amount. Each line or group, however, must be watched by the retailer or the salesmen to see that the proper assortment of goods is on hand. Owing to this

limitation, dollar control is seldom used in smaller stores. In larger stores it is an excellent method of controlling the buyers and keeping the stocks of the various departments in balance. The manager can quickly spot any lines that have too many or too few goods. Too much capital is not tied up in one line while the stock of another line is depleted.

Taking inventories. Stores using a tickler system or a perpetual inventory system must take inventories frequently. For example, stocks may be taken monthly with a tickler system, and quarterly or semi-annually when a perpetual inventory system is used. In taking stock under a tickler system or under the unit system of perpetual inventory, only the number of items in stock (including those out on approval) need be entered on the stock records. It is usually better to have one man call off the number of articles in stock and another to enter them on the record. If stock is properly arranged, it can be inventoried in periods when there are no customers in the store.

A device that may prove helpful in some stores is a dictaphone, connected to a wax cylinder. The stocktaker calls the number of items into it. The cylinder may be played back by a stock clerk later; or the stock clerk may have earphones and make the entries on the stock records as they are called. If the inventory is to be accurate, care must be taken to include goods in reserve stock as well as merchandise in the salesroom, also goods out of the store on approval.

Valuing inventories is necessary when profit-and-loss statements are to be prepared at the end of fiscal periods. With a model stock plan, the cost price and often the selling price are on the stock records. The value of the inventory can be computed from these figures. If the inspection system is used, and the cost prices have been entered on the price tags, the cost may be transferred to the stock sheets. If the cost prices are not carried on the price tags, they must be secured from invoices.

Stock Turnover

The rate of stock turnover measures the length of time goods are kept in stock before they are sold. A turnover of 2 indi-

cates that the stock is turned twice a year and that the goods are kept in stock for six months. A turnover of 4 means that they are kept in stock for three months. The turnover figure for a store is an average. Though a store has an average turnover of 2, it may have some articles that turn only once in two or three years while other items turn every month. Some off-sizes or some seasonal items may turn less than once a year while some staple items may turn over monthly. If a retailer wishes to increase his average turnover, he may do so by installing a better stockkeeping system and by adding more fast-turning lines to his stock.

Method of computing rate of stock turnover. The rate of stock turnover is computed by dividing the cost of goods sold by the average cost value of the goods on hand. The cost of goods sold is the amount of goods on hand at the opening of the fiscal period, plus the purchases made during the year, less the goods on hand at the end of the period. Here is an example:

Inventory on hand, January 1	$15,026
Purchases made during the year	32,256
Total goods on hand during the year	47,282
Inventory on hand, December 31	15,211
Cost of goods sold	$32,071

The average inventory is computed as follows:

Inventory on hand January 1	$15,026
Inventory on hand December 31	15,211
	$30,237

$$\frac{\$30,237}{2} = \$15,118.50 \text{ average inventory}$$

$$\frac{\text{Cost of Goods Sold } \$32,071.00}{\text{Average Inventory } \$15,118.50} = 2.1 \text{ rate of stock turnover}$$

The stock was turned 2.1 times during the year. In other words, it required 174 days to turn the stock. This means that, on the average, an article was in stock 174 days before it was sold.

Methods of increasing the rate of stock turnover. The rate of stock turnover can be increased by the following methods:

1. Reducing the inventory while sales remain the same
2. Reducing the inventory while sales increase
3. Reducing the inventory faster than sales decrease
4. Increasing the sales while the inventory remains the same
5. Increasing the sales faster than the inventory increases.

The inventory may be reduced by decreasing the number of slow-selling items or by continuing to handle the same variety of items but carrying a smaller number of each of them. This plan may lead to buying more frequently and in smaller lots. It can be an uneconomical method of buying and thus defeat the object of a faster rate of stock turnover.

When a retailer studies his sales he usually finds that he stocks many slow-selling products. This may arise from carrying duplicate brands, or from carrying sizes which are in little demand. The majority of the sales of an article are usually in a relatively few sizes. The other sizes may be discontinued, although this will inconvenience the few buyers who request them. If a retailer finds that many items sell so slowly that they involve a loss, he might discontinue them and use the capital and space for items that sell faster.

The retailer can increase his rate of turnover without reducing the number of articles stocked by keeping a smaller number of each on hand. To accomplish this he must have a stock-keeping system that informs him when to place orders. Without such a system he will be out of stock too frequently. It is also helpful if he can buy from a nearby jobber and receive his merchandise quickly.

Some retailers increase their rate of stock turnover by increasing their sales. This may be done by lowering prices, by better window and store displays, by more advertising, and by better salesmanship. The "merchandising" store often utilizes price leaders to increase sales with the idea of reducing its percentage of expenses by means of a faster turnover.

The advantages and limitations of a rapid rate of stock turnover. From time to time it has been pointed out that a rapid rate of stock turnover has certain advantages. It has been

pointed out that a rapid rate of stock turnover usually decreases operating expenses and increases profits, that more cash discounts can be taken, and that goodwill is created by always having on hand what the customer desires.

It cannot be said with certainty that a rapid rate of stock turnover is the sole cause of these benefits. A large number of sound retailing practices, some of which are but indirectly connected with the speed of sale and the investment in the inventory, create these advantages. A more rapid rate of stock turnover is associated with efficient operation but is not the cause of efficient operation. It is possible to have rapid rate of stock turnover and still operate at a loss. In periods of declining prices the rate of stock turnover may be increased but losses may increase faster.

The expenses of interest, rent, heat, light, depreciation on fixtures, taxes and insurance are incurred in carrying a stock of merchandise. Some retailers point out that they cannot obtain a rent reduction or move to a smaller building with lower rent just by reducing the size of the stock. Due to other conditions it may not be possible to reduce the expenses of interest, insurance, and taxes. If a retailer does not move to a smaller building, he may take more cash discounts on his purchases or he may use the capital released by a faster rate of stock turnover to add other lines to his stock. These lines may increase his sales so that his percentage cost of rent, heat, and light will be reduced. He may have fewer soiled or obsolete articles which must be sold at a loss. None of these, however, are necessarily a result of a more rapid rate of stock turnover. If, in an attempt to obtain a more rapid rate of stock turnover, the inventory is reduced too much, the risk of lost sales is incurred. When a customer asks for an article and it has been discontinued or is "on order," the sale is lost and perhaps also the future patronage of the customer.

Eliminating slow-moving items. The rate of stock turnover may be increased by eliminating the slow-selling items—the sleepers, the shelf-warmers, the boarders. To prevent an accumulation of such items, the stock should be inspected closely from time to time with this purpose in mind. When in doubt,

invoices and inventory records may be examined. Some articles sell very slowly but the fast-moving items might sell less rapidly if all slow movers are eliminated.

The problem with sleepers is to determine which should be continued in stock and which should be closed out. Perhaps some are sleepers because they are not displayed. The consumers may not know that the store sells the product. They may be buying it elsewhere. The problem with such products is to give them sufficient display and advertising. Other shelf-warmers may actually be in such small demand in the community that the store should close out its stock. There will be some slow sellers that the dealer feels he should carry as a part of his service to the community, even though they slow up his rate of stock turnover. The longer an item is carried in stock the greater the expense. When a slow-selling product is carried, the retailer should consider its selling price. It may be that it will bear a larger than usual margin and thus cover the extra expense. If this can be done, it may be handled profitably.

Questions

1. What are the benefits of stock control?
2. What are the three general methods of controlling stock?
3. What are weaknesses of the inspection system of stock control?
4. What may be done to make the inspection system more successful?
5. When is labeling a minimum quantity impractical?
6. What is the tickler system of taking frequent physical inventories?
7. What is a perpetual inventory system? How is it operated? What information will it provide?
8. If a retailer has an opening inventory of $8,000, a closing inventory of $6,000, and during the year has purchased $28,000 worth of goods, what is his rate of stock turnover?
9. What are the five different methods of increasing the rate of stock turnover?
10. Is a rapid rate of stock turnover a cause of certain benefits? Explain.
11. Which system or systems of stock control are adapted to the needs of the following types of retail stores: large department

stores; large hardware stores; medium-sized drug stores; small grocers; medium-sized shoe stores; small women's clothing stores; small men's furnishing stores?

12. Which system is adapted to the needs of a wholesale grocer? A wholesale hardware dealer?
13. MacMillan Bros. conduct a retail hardware store in a town of 5,000 population. They have taken stock only once a year, and they depend upon inspections of the stock or want slips to tell them when they should order additional goods. The traveling salesmen often inspect their shelves and tell them what they need in their lines. They have many more goods than they need, their turnover being very little more than once a year. In spite of this, they must often tell customers that the desired goods are out of stock. It often happens that the goods are actually in the store or stockroom but are misplaced or hidden under other goods. The brothers realize their entire stock-keeping system needs improving.

    They ask you to work out a tickler system adapted to their needs. Describe the system which you would recommend and draw up the necessary stockkeeping forms. How would you go about setting up or determining their model stock?
14. Johnson & Edwards, Inc., operates a men's clothing store. They want to install unit control for suits, overcoats, and shoes, and dollar control for their furnishings.
    (a) Draw up the proper system for their coats and suits, showing samples of any stockkeeping forms needed.
    (b) Do the same for their shoes.
    (c) Do the same for their furnishings.
    (d) Show how they should determine their model stocks.
15. Is it possible for a dealer to carry full assortments of goods and at the same time turn his stock rapidly? Discuss. Does the answer to this question depend somewhat upon the dealer's location and his volume of sales?
16. How does the amount of goods necessary to satisfy customers vary with the type of merchandise? With the type of customers?
17. Why do so many dealers "take stock" (an inventory) only once a year? Is this a good practice? Why or why not?
18. Should inventories be taken when the inventory is high or when it is low?
19. The store with a complete stock of goods often has a slow rate of turnover and high expenses. It is hard for such a store to meet the prices of stores with a limited stock and a quick turnover. Under what conditions should a dealer carry a large number of articles in stock, if this means relatively high operating expenses?

20. It has been proposed that the retailers in the smaller cities (say in cities of under 50,000 population) form a working agreement as to the lines of goods that each will carry. One shoe dealer might agree to carry a full line of narrow shoes; another, a complete line of wide shoes; a third, a full line of arch support shoes. The stationery store might agree to discontinue sporting goods, while the sporting goods store would agree to discontinue radios and musical instruments, and the music store to discontinue books and magazines. In this way the town would have complete lines of all classes of goods and so serve its customers better. The convenience and availability of the goods would draw more trade from the surrounding territory and so increase the city's trading area.

Evaluate this proposal. What are some of the difficulties to be faced in securing and maintaining such an agreement?

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Merchandising Efficiency

THERE are several tests for determining the operating efficiency of a retail business. One of the most important is the amount of profit made during a given period. It is desirable to know, however, the specific causes of the profit or the reasons for the lack of it. To determine this, the retailer investigates the efficiency with which he uses the labor he employs and the capital he has invested. He analyzes the costs of his operations.

Some of the various tests for merchandising efficiency have been discussed earlier. These are the collection percentage, the determination of net profit and profit by lines, and the rate of stock turnover.

Testing for Operating Efficiency

How can a retailer determine if his operating expenses are too high? He can compare them with the average for a group of similar stores and find out if his expenses and profits are above or below average. If they are above average, he can strive to bring them down to average. Some retailers are not satisfied to be "just average"; they prefer to be better than average. Such retailers will try to reduce their expenses until they are below the average of similar stores. For this reason, some organizations publish figures for better-than-average stores, or for profitable stores.

The National Retail Hardware Association, for example, publishes figures of average margins, expenses, and profits for

hardware stores of various sizes located in towns of various sizes. The size of the town is important because the expense percentage increases with the size of the town in which a store is located. This association also publishes average figures for the profitable stores.

Analysis of operations. A comparative analysis can be illustrated by using the information compiled for Johnson's Hardware Store. The table includes the average of all reporting stores and all profitable stores with sales of between $40,000 and $60,000 located in towns of over 50,000 population.

It will be seen that Johnson had a higher margin than the average of all stores but a slightly lower margin than the average of the profitable stores. Johnson's expenses were below those of the other two groups. He made a larger percentage of net profit than either group. He took fewer cash discounts, however, than average. When this was added to his net profit he still had a higher-than-average rate of net earnings but a rate slightly below the average of profitable stores. When his earnings were compared with his investment, he made a considerably higher-than-average return but slightly less than the average rate made by the profitable stores.

Johnson, however, paid himself a higher salary than did most merchants with stores of similar size. If he had taken an average salary and added the difference to his profit, his return on his investment would have been 17.7 per cent, much higher than the average of the profitable stores. Johnson's earnings and salary combined amounted to $4,687.

Johnson's expenses were 2 per cent below the average and 0.3 per cent below the average of the profitable stores. When we look at his expenses in detail we find that most of the saving was in the salaries of his salesmen. Some of his other expenses were low and some high. His advertising expense was average. His delivery expense, taxes, and rent were considerably below average. Interest on borrowed money, bad debt losses, and "other" or miscellaneous expenses were relatively high.

The reasons for all of these variations are not apparent from his statement. His low selling expenses may be due to low salaries or to the greater use of part-time salesmen. He also

does outside selling and may charge the salesman's expenses to travel. If so, some selling expenses are in the other expenses. Whatever the reason, his percentage cost of selling is low and this is reflected in higher profits.

COMPARISON OF JOHNSON'S HARDWARE STORE WITH AVERAGE AND PROFITABLE STORES OF SIMILAR SIZE IN TOWNS OF OVER 50,000 POPULATION

	OTHER HARDWARE STORES		JOHNSON'S STORE	
	Percentages		Dollars	Percentages
	All stores	Profitable stores		
Sales	100	100	$45,869	100
Cost of goods sold	70.3	69.8	32,071	69.9
Gross margin	29.7	30.2	13,798	30.1
Expenses:				
Salaries—owners	3.1	2.8	1,820	4.0
" selling	10.1	9.5	3,158	6.9
" other	1.8	1.7	817	1.7
" total	15.0	14.0	5,795	12.6
Advertising	1.1	1.0	505	1.1
Delivery	2.15	1.85	248	.5
Rent	4.3	4.3	1,429	3.1
Insurance	.5	.5	346	.75
Taxes	.9	.7	190	.5
Interest on borrowed money	.3	.3	213	.5
Bad debts	.45	.4	571	1.2
Other	2.0	1.95	2,031	4.45
Total expenses	26.7	25.0	11,328	24.7
Net operating profit	3.0	5.2	2,470	5.4
Cash discounts taken	1.2	1.3	399	.9
Net earnings	4.2	6.5	2,869	6.3
Rate of stock turnover	2.4	2.4		2.1
Net earnings, per cent of investment	10.4	15.8		14.9

Johnson does little delivering. He has a neighborhood location and most of his customers carry their purchases home. He carries fire, burglary, workmen's compensation, public liability, automobile, and contractor's liability insurance; some dealers

do not carry all these forms. He apparently borrows more money than most retailers of his size, which is, at least partly, explained by the fact that he has less capital invested than do most hardware dealers with his volume of sales.

Johnson's bad-debt losses were unusually high. We are not able to compare his credit sales with the average so we cannot say whether it is caused by larger credit sales, sales to poorer risks, or lax collections. It may be a combination of all three, or perhaps it results from more installment sales of appliances. If caused by lax collections, he should correct the situation.

"Other" expenses are high chiefly for two reasons: high traveling expenses and heavy expenditures for supplies. The travel expense may include the automobile expense of an outside salesman and Johnson's own traveling expenses on buying trips. The inclusion of traveling expenses with selling expenses would increase the latter slightly. Johnson has more expense when buying because he makes intense searches for merchandise and often picks up some "special buys." He also buys more goods "direct" than do most stores of this size. He also spends relatively large amounts for store supplies—materials used in servicing appliances.

The cash discounts taken were below the average. The low figure may be due to carelessness. On the other hand, some of his lines and "special buys" carry low rates or no discount. The fact that he has less capital than some stores may cause him to miss the discount on some invoices. If he misses cash discounts because of carelessness, the situation should be corrected.

Johnson's rate of stock turnover is below the average for similar stores. This may be because he makes more direct purchases or buys "job lots." However, the lower rate may also result from poor stockkeeping.

To sum up, Johnson has somewhat lower expenses and somewhat higher profits than most of the profitable stores located in towns of more than 50,000 population. The analysis of his operations, however, does indicate where he could reduce his expenses. For example, his bad-debt losses are very high, and his rate of stock turnover might be improved. Although the salaries of his salesmen are relatively low, this is largely offset

by high traveling expenses and a high expense for store and office supplies.

Any retailer can compare his operations with some standard. It may be the average figures for similar stores, or it may be a considerably higher standard, perhaps the most efficient one-fourth or one-tenth of the dealers. Dun & Bradstreet, Inc., publish figures for average and profitable stores of various sizes located in different-sized towns.

Reducing expenses. Sometimes an analysis of the retailer's operations will show that his margin is too low, but in the majority of situations the best way to increase profits is to reduce expenses.

An inexperienced man purchased a small neighborhood store. He knew nothing about average expenses but he kept his expenses and prices low. Eventually he became one of the more successful retailers in his section of the country. The first key to his success was keeping his expenses considerably below the average. He could sell at attractive prices and at the same time make satisfactory profits. The second key has been full and complete stocks. The third key has been liberal service, particularly delivery and credit service. The fourth key has been active sales promotion.

"Suppose I find that my expenses are high? How can I reduce them?" asks a retailer. Realizing that expenses are too high is important. Once a retailer knows the situation he can search for ways of reducing them.

If a retailer has high selling expenses, it may be that the volume of sales per salesman is low, or that he is paying higher than average salaries. If the sales volume per salesman is low, he may need fewer and/or better salesmen. Perhaps his sales training program is not adequate; or he has more salesmen than he needs. He may be able to reduce expenses by hiring part-time salesmen for busy periods and employing fewer full-time salesmen.

Perhaps he has a poor layout that causes wasted steps and lost time in locating merchandise. If so, he should rearrange his store. One definite method of approaching the problem of high selling expenses is to encourage customers to wait on themselves

and bring their selections to the cashier. Despite the fact that there is some loss due to the theft of small articles, and some expense because stocks must be carefully arranged, marked, and maintained, a considerable saving in selling expenses can be made.

Percentage selling costs tend to be high on small items, as the amount of time required to sell them is high in proportion to their value. A store may add higher priced articles on which the percentage selling expense is lower.

If the percentage cost of rent is high, the retailer should examine his location and determine if he is paying more than it is worth. If so, perhaps he can negotiate for a reduction in rent, or move to a building where the rent is less. Perhaps the location is worth the rent he is paying but is too expensive for his line of goods. In this case he may be able to dispose of the building by subleasing it and to move into a lower rent district. Another solution would be to add lines of goods which will sell fast enough, or at a high enough margin, to pay the high rent.

Rent may be high because the store has too much space for its volume of sales. If this is the situation the dealer may strive to increase his sales by adding additional lines, or by stimulating sales of present lines by better window displays and more advertising, or by outside selling. Perhaps the building needs new display windows. Another solution is to sublease a part of the space. The second floor or basement may be rented and a separate entrance provided. Again, the main floor may be subdivided or part of it leased to a retailer who will handle an allied or complementary line.

If the retailer finds that his bad-debt loss is above the average, it probably indicates either unwise extension of credit or lax collection methods. These faults should be corrected.

On the other hand, his bad-debt loss may be too low, a situation which indicates that he is perhaps too strict in granting credit or that he pushes collections too hard. Actually, he may be limiting his sales and profits. A retailer should determine the percentage of losses which he expects and can afford to take. This percentage varies. One store may choose a liberal credit

policy, take a large margin (high markups), and expect a fairly high bad-debt loss. Another store may elect to keep its prices low. To make a profit it has to watch its expenses closely; therefore, it cannot afford large bad-debt losses.

Once the standard is set, the retailer should watch the percentage closely. If it goes too high, he should accept fewer borderline risks and push collections on his poorer risks more closely. If his bad-debt percentage drops too low, he should accept more borderline risks, or he should be somewhat more lenient on accounts less than 30 or 60 days past due.

The same procedure may be followed in analyzing other expenses and trying to reduce those that are too high.

The Use of Capital

Even in a small store several different assets are needed in order to operate the business. Most new enterprises have only limited funds to invest. It is important that these funds be used carefully and that only those assets be bought which will contribute most to success. Furthermore, the amount of each asset should be kept proportional to the need. The two major questions which must be answered are: What assets are required? And how much of each asset is needed?

The assets of a store are the salable merchandise, store equipment and fixtures, customers' accounts receivable (if a credit business is done), store supplies, and some cash with which to meet day-to-day expenses and to provide a reserve for unexpected needs. A building is also needed in which to do business, but the new merchant usually rents the necessary space and uses his own limited resources for other things.

The amount and kind of each asset needed depend on the volume of business done, and the way the business is operated. For example, a delivery truck is needed if the business emphasizes its delivery service, and accounts receivable must be carried if the store offers a credit service.

Most of the funds needed to start a new business should be provided by the owner or owners. The initial capital furnished by the owner may come from savings already on hand. The

owner's investment is really long-term capital and is presumably to be left in the business permanently. The creditors of the business rely upon it to protect their loans to the business.

Often the owner will supplement his savings by borrowing a portion of his initial investment. Loans of this sort may be obtained from friends or relatives. But since the funds are presumably to be left in the business there should be a clear understanding that the loans will not be repaid for some years. If the business is incorporated, friends or relatives can be given stock in return for the funds they invest initially in the new business, perhaps with the promise that the owner will buy it back if they wish to sell. This agreement gives the arrangement some of the characteristics of a loan rather than of an investment in the business.

Long-term loans may also be obtained from insurance companies, mortgage loan companies or other financial institutions. Collateral in the form of insurance policies, real estate, or other property is usually required as security. When the owner borrows on the security of property he already owns, the net result is similar to the sale of assets. He, in effect, gets cash for an asset he already owns; but he retains control of this asset.

The most common sources of short-term loans are the wholesalers and manufacturers who supply goods on credit, and the bank which loans on unsecured or secured notes or on notes signed by an accommodation endorser. These loans are primarily for operating purposes rather than for initial capital. After the business is established it sometimes may be possible for the owner to borrow on its assets or to buy these assets with the help of credit. If the business includes real estate, he may obtain a long-term loan secured by a real estate mortgage. He may also borrow on the furniture and fixtures and secure the loan by a chattel mortgage.

Many retailers have been financed chiefly in their early days by wholesalers. The latter have extended substantial credit for long periods to men who they felt had ability, honesty, and industry and who would succeed. The new retailer should not, however, depend on very much credit from wholesalers until he has his business well started. A beginning retailer should

have enough money of his own, or borrowed for long terms, to pay for the opening stock, to make a substantial payment on the fixtures, and to provide enough cash to cover operating expenses for some months. True, numerous successful businesses have been started on less, but many of those who have tried to operate on a shoestring have failed. It is well when starting a new business to finance soundly and thus have a safety margin.

Typical balance sheet. The following is the balance sheet of Johnson's Hardware Store. This illustrates how a going business has managed its financial affairs.

ASSETS			
Current assets:			
Cash on hand	$140		
Cash in bank	275	$ 415	
Accounts receivable		6,690	
Merchandise inventory		15,211	
Total current assets			$22,316
Fixed assets:			
Furniture and fixtures	$1,671		
Less reserve for depreciation	429	$1,242	
Delivery equipment	515		
Less reserve for depreciation	64	451	
Total			$ 1,693
Total assets			$24,009
LIABILITIES			
Current Liabilities:			
Accounts payable	$2,091		
Notes payable	2,700		
Total			$ 4,791
Net worth			19,218
Total			$24,009

During the year, sales amounted to $45,869 and purchases amounted to $32,256.

Current, or quick assets, consist of cash or of other assets that can be converted into cash quickly. A retailer usually has

current assets consisting of cash, merchandise, accounts receivable, and sometimes of notes receivable. Notes receivable are often taken on the sale of large articles such as farm equipment, refrigerators, and washing machines. Such notes may be carried by the retailer, discounted at the bank, or sold to a finance company. Apparently Johnson did not take any notes; if he did, he sold them.

Fixed assets are those needed permanently in the operation of the business. As a rule, they can not be turned into cash quickly, even in an emergency, if the store is to continue in business. The usual fixed assets of a retail merchant are furniture and fixtures in the store, delivery equipment, and real estate, if the building is owned. Johnson did not own his building, and so had only store equipment and fixtures and a delivery truck as fixed assets.

The relation of current assets to current liabilities is known as the current ratio. A store in a sound financial condition should usually have current assets twice as large as its current liabilities. A store with a lower ratio may have difficulty in borrowing from a bank. Current assets are converted into cash in the normal operations of the business. Cash, of course, is a current asset. The retailer's debts come due and must be paid, but his assets may be convertible into cash slowly. If he must have cash quickly, he may realize less than their face value. Therefore, to have a margin of safety, current assets should exceed current liabilities. Merchandise is sold either for cash or for credit. If sold on credit, the account must be collected to obtain cash. Accounts receivable are therefore said to be more liquid than goods in stock because they are one step nearer to cash. Johnson is in a very strong current position. His current assets ($22,316) are almost five times (4.6) his current liabilities ($4,791).

If Johnson decided to expand his business, he could buy $12,000 more goods on credit without causing his current ratio to drop below 2 to 1. If he bought this amount of goods, his current assets would be $34,316, his current liabilities $16,791 and his current ratio 2.05 to 1.

Johnson's current liabilities consist of accounts payable for

merchandise and notes payable. Apparently he has borrowed at the bank to obtain funds with which to take the cash discount on his purchases.

The value of the fixtures is less than 3 per cent of annual sales. Johnson has no fixed liabilities, those liabilities which do not become due until a much later date. The more usual ones are mortgages on real estate or, in the case of corporations, bonds. If a bond or mortgage is coming due within a year, it should be treated as a current liability.

The difference between total assets and total liabilities is the owner's capital, or net worth. For Johnson, this amounts to $19,218. If this store were a partnership, the net worth would be divided between the partners. If it were a corporation, it would be shown as capital stock outstanding, perhaps belonging to a number of people. Johnson's net worth is four times as large as his debt. This is above the average and shows that Johnson is in a strong capital position.

Johnson paid himself a salary of $1,820. His earnings, after paying expenses, including his salary, depreciation of fixed assets, and interest paid on borrowed money were $2,869, or 6.3 per cent of sales and 14.9 per cent of the capital invested in the business.

Establishing a line of credit. It is most important that the new retailer establish credit with his bank and with wholesalers. The best way to do this is to pay all bills on time. As a basis of credit, one needs some capital, some earnings, and a good reputation for honesty and ability. If a store is established on a cash basis, it indicates that the retailer has some capital. If the store is successful, the retailer demonstrates that he has ability. Establishing the fact of his honesty is the next step. This may be done through references to people who have known him in the past, and who will vouch for his conduct and reputation in the community where he lives. The retailer then buys some goods on credit and pays for them as agreed. Thus he establishes his credit with a few sellers. The latter can then be given as references when credit from others is desired.

The best time to establish credit is when one is able to pay, that is, when business is good. It is said that Andrew Carnegie

as a young man borrowed money he did not need and paid interest on it in order to establish his bank credit so that he could borrow money when he did need it. When funds are needed most acutely, the balance sheet probably makes the poorest showing. If a retailer establishes a regular line of credit when his financial position is strong, he is more likely to secure credit when funds are needed most.

Use of assets in general. We have discussed above the financial organization of one typical hardware store. Let us now look at the use of assets by hardware stores in general. The use will vary widely from one store to another depending on (1) whether or not the retailer owns his building, (2) how much credit he extends, (3) how closely he collects his accounts, (4) how rapidly he turns his stock, (5) whether or not he has his own delivery equipment, and (6) how much he invests in furniture and fixtures, and how new they are.

Reports from a large number of hardware stores show that their assets are equal to between 50 and 60 per cent of their annual sales. The average of these reports show that the relative importance of assets and liabilities are about as shown below, expressing total assets as $100. When expressed in percentages, such a statement is called a hundred-per-cent statement.

BALANCE SHEET OF AVERAGE HARDWARE STORE

ASSETS			LIABILITIES	
Cash	$ 2			
Accounts and notes receivable	22		Accounts and notes payable	$ 15
Merchandise inventory	58			
Total current		$82		
Furniture and fixtures	$ 6		Net worth	85
Delivery equipment	2			
Land and building	10			
Total fixed		18		
Total assets		$100	Total liabilities	$100

The above figures are average. The reports of individual stores will vary widely. If a store sells for cash, it would have no receivables and this would change the relative importance

of the other assets. If a store sells some of its notes receivable, it may have less money invested in receivables than shown above. If a store sells on thirty-day credit terms and collects its accounts with reasonable promptness, it will have less money tied up in receivables than is indicated by the figures in the above table. However, if a store makes most of its sales on credit and is slow in making collections, it may have a larger proportion of its capital invested in receivables.

The amount of capital invested in a stock of merchandise will vary with the rate of turnover. A store with a rapid rate of stock turnover but with a liberal credit policy may have a smaller proportion of its capital invested in merchandise. On the other hand, a store with a slow rate of turnover will have relatively more goods in stock.

A store that has just bought and paid for new fixtures will have a larger part of its assets in furniture and fixtures than another store that has written off most of the value of its fixtures as depreciation. A store may write off its fixtures entirely in ten years and yet if they are not obsolete, find that they are good for several additional years.

A store that has no delivery truck will not have this asset on its books, but a store that features delivery service and has just purchased new trucks will have some capital invested in delivery equipment.

AVERAGE BALANCE SHEET FOR A HARDWARE STORE RENTING ITS BUILDING

ASSETS			LIABILITIES	
Cash ($2–$3)	$ 2.50			
Receivables	23.00		Payables	$ 15.00
Inventory	65.00		Net worth	85.00
Total current		$ 90.50		
Furniture and fixtures	$ 7.50			
Delivery equipment	2.00			
Total fixed		9.50		
Total assets		$100.00	Total liabilities	$100.00

Only about one-third of the hardware stores own their buildings. In the above balance sheet the value of real estate is an

average figure and thus much smaller than it would be for a store owning its building. When a retailer owns his own building, other assets will be relatively smaller, although they may be as large in relation to the store's sales as they are in the above balance sheet. Since two-thirds of the stores rent their buildings, it may be well to show how their assets are distributed.

A store without an investment in a building can carry more stock and receivables and make larger sales with a given capital than can a store that has a substantial part of its capital invested in a building.

The chief liabilities of a store are merchandise accounts payable to wholesalers and manufacturers; notes payable to banks for money borrowed with which to pay for goods or to pay expenses; chattel mortgages or liens given on the purchase of furniture and fixtures, or delivery equipment; and, if the building is owned, a mortgage on it. Other liabilities may include bills payable for wages or other expenses and occasionally a judgment for injury or damages.

Contingent liabilities are potential liabilities that do not become real unless certain contingencies happen. A retailer may endorse notes for others. If the maker does not pay, the endorser is liable. A retailer may take notes in payment for goods or debts. If he discounts these at the bank, he usually is required to endorse them. If not paid by the maker, the merchant is liable to the bank. Again, if a retailer is sued for some damage, the suit may be considered a contingent liability until settled because the retailer may lose the suit and be held liable for damages. This contingency is often covered by insurance.

Seasonal variations. The relative importance of a store's assets and liabilities will vary with the seasons. Stores having their largest sales volume in the spring buy merchandise in advance of this season, thereby increasing the inventory and accounts payable. During the spring months, many of these goods will be sold for cash and on credit. The merchandise inventory will decrease, accounts receivable will increase, and cash should increase until used to pay some of the bills, when it will decrease. In order to take the discounts, the retailer will very often borrow money at the bank. Thus, his accounts

payable will decrease and notes payable will increase. As he collects from his credit customers his accounts receivable and his notes payable will decrease.

If the store has a small sales peak in the fall, the above changes may take place on a smaller scale. The store with large sales to farmers may find its collections are made chiefly in the fall. Thus, as winter approaches, the accounts receivable may drop to their minimum. The same should be true of both accounts and notes payable. Cash will tend to be larger than at other seasons. Certain types of stores have a large sales volume in December and a small volume in July.

Questions

1. How can a retailer determine if his operating expenses are too high?
2. What is the relation between the volume of sales per salesman and a retailer's expenses and profits? Why this relationship?
3. Why does the average volume of sales per salesman vary so widely in different types of stores? In similar stores selling the same kind of merchandise?
4. How can a retailer increase the average volume of sales made by his salespeople?
5. What is the relationship between the arrangement of goods in a store and the volume of sales per salesman?
6. What is the disadvantage of occupying too much space? Too little space?
7. What relationship does store location have to rent costs?
8. Should the bad-debt loss percentage be computed on total sales or on credit sales?
9. What is the relation between the prompt collection of accounts receivable and expenses?
10. What is the relation between bad-debt loss and credit policy?
11. What are the sources of short-term capital for a retailer?
12. What are current assets? Fixed assets?
13. Define the term *current ratio*.
14. How will the following affect a retailer's assets
    a. Selling on credit
    b. A lax collection policy
    c. Constructing his own store fixtures
    d. Not delivering
    e. Renting the store building
    f. Carrying only fast-moving items

15. What are contingent liabilities?
16. How do a retailer's assets and liabilities vary with the seasons? Does the variation occur at the same time for all retailers?
17. The Dependable Furniture Store is operated by Mr. Charles Kirk. His sales for the year are $40,000 of which $12,000 was on credit. During the year he purchased merchandise with a cost value of $23,000. On January 1 he had on hand merchandise which had cost him $16,000. At the end of the year the cost value of his inventory was $14,000. During the year he paid himself a salary of $5,000 and he paid others who worked for him wages of $4,200. His advertising cost amounted to $1,000, his delivery expense was $800, his taxes were $400, and the cost of his insurance was $240. He paid the bank $120 for interest on money borrowed and his bad debts for the year amounted to $400. Miscellaneous expenses amounted to $640. He pays $100 rent per month for the building in which he is located.

    At the end of the year he has $1,200 cash on hand and customers owe him $2,000. He values his store equipment at $2,000 and his delivery equipment at $2,500. He owes manufacturers and wholesalers $2,500 and the bank $3,000.

    Compute the following:

    a. percentage of cost of goods sold
    b. percentage of gross margin
    c. percentage of each expense
    d. percentage of total expenses
    e. percentage of net profit
    f. rate of stock turnover
    g. current ratio
    h. net worth
    i. net earnings on investment
    j. percentage of credit sales which were collected.

18. The Starr Clothing Company, operated by J. B. Starr, has sales for the year of $36,000 of which $15,000 worth were on credit. During the year he purchased merchandise which cost $22,000. On January 1, the stock on hand had a cost value of $20,000 and at the end of the year it was worth $18,000. Mr. Starr paid himself a salary of $300 per month and others were paid $2,400 during the year. He spent $1,000 for advertising and his taxes amounted to $300. He paid the bank $100 interest on money he had borrowed and his insurance cost him $200. Losses on bad debts amounted to $200 for the year and his miscellaneous expenses were $600. He pays $125 rent per month for the building he occupies.

    At the end of the year he has $1,800 cash in the bank and in

his safe. Customers owe him $1,500 and he values his store fixtures at $3,000. He owes manufacturers and wholesalers $3,000 and the bank $2,000.

Compute the following:

a. percentage of cost of goods sold
b. percentage of gross margin
c. percentage of each expense
d. percentage of total expenses
e. percentage of net profit
f. rate of stock turnover
g. current ratio
h. net worth
i. net earnings on investment
j. percentage of credit sales which were collected.

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The Problem of Insurance

A BUSINESSMAN talking about education said that one thing he learned in class one day more than paid for all his expense in going to college. He said he learned that certain risks should never be carried but should always be shifted to an insurance company. When he entered business he saw such a risk and increased his insurance to the full value of the building. He suggested to the man owning adjoining property that he do the same, but this man said "those buildings will never burn," and did not increase his insurance. The buildings did burn. The first man got enough from his insurance to replace his property completely while the second man's insurance did not nearly cover the cost of rebuilding.

Most of us know too little about the risks of operating a business, which risks can be covered by insurance and which should be covered. If a retailer purchased all the insurance available, he would be heavily overinsured. On the other side, many retailers become bankrupt because they do not have enough of the proper kinds of insurance. The retailer should determine the risks in operating his business and then should ascertain the various kinds of insurance available to cover them. With this information it is possible to select and buy insurance with some degree of wisdom.

Determining Risks

Risks vary with location, type of building, kind of business, method of operation, and goods handled. The following list

indicates most of the insurable risks involved in operating a retail business.

1. Cash

   Loss by:

   - Fire
   - Interior robbery
   - Outside robbery (on way to bank or from a collection)
   - Messenger robbery
   - Burglary of safe
   - Embezzlement
   - Check alteration
   - Forgery
   - Burglary of safety deposit box

2. Government and Other Marketable Securities

   Loss by:

   - Fire
   - Interior robbery
   - Messenger robbery
   - Embezzlement
   - Burglary of safe
   - Burglary of safety deposit box

3. Accounts Receivable

   Loss by:

   - Burglary of records
   - Destruction of records by fire

4. Notes Receivable

   Loss by:

   - Fire
   - Burglaries
   - Robberies

5. Merchandise

   Loss by:

   - Fire
   - Burglary
   - Robbery
   - Theft

   Damages by:

   - Smoke
   - Smudge

Damages by (Continued):

Water
Accidental operation of automatic sprinkler
Steam
Flood
Explosion
Electric current interruption

Liability on account of injury:

Arising from the sale of merchandise

6. Delivery Equipment

Loss by:

Fire
Theft
Collision
Explosion

Damage by:

Fire
Theft
Collision
Explosion

Liability on account of:

Injury to employees and others
Damages to automobiles and property of others

7. Furniture and Fixtures

Loss by:

Fire
Theft
Burglary

Damage by:

Fire
Theft
Burglary
Explosion
Water
Flood
Smoke
Smudge
Accidental operation of automatic sprinkler, heat, or water systems

Liability on account of:

Accidents to employees and customers

8. Building and equipment

Loss by:

Fire	Windstorm
Tornado	Lightning
Explosion	Cancellation of lease

Damage by:

Fire
Tornado
Explosion
Windstorm
Lightning
Operation of automobiles by others
Flood
Accidental operation of sprinkler, plumbing and heating system
Breaking of display windows
Breakdown of engines and electrical equipment
Failure of elevators

Liability on account of:

Acts of contractors and their employees
Injury to customers caused by falling plaster, bricks, slate, glass signs, snow, fire escape ladders, and by defective railings
Failure of elevators
Explosion of boiler

9. Land

Loss of title.

It is certain that some retailers will suffer losses from these risks but it is impossible to predict definitely when or where a loss will occur. Against which of these risks should a merchant carry insurance? One standard for answering this question is the frequency with which losses occur. Because fires occur frequently, most retailers carry some fire insurance.

A second standard used in determining the insurance needs of a retailer is the severity of the loss which would result in the event a given contingency occurred. If the loss would cause a serious impairment of the assets of a business such as an extensive fire, then insurance is needed to cover the contingency. If the occurrence of a given event would result in a serious impair-

ment of earnings for a long period, it would seem wise to insure against such a loss. Most retailers do not appreciate the loss of earnings which occurs in the period of business interruption following a serious fire. Such a loss of profits is not covered by the standard fire policy, but it may be covered by business interruption insurance.

A third standard is the cost of the insurance. If the insurance premium is an appreciable proportion of the loss which might occur, then it may be well for the merchant to carry the risk and forego insurance.

Insurance Against Loss by Fire

Cash and marketable securities. The retailer's most liquid assets can not be protected by fire insurance. The standard fire policy specifically excludes "accounts, bills, currency, deeds, evidences of debt, money, notes or securities." Thus the balance-sheet items of cash, marketable securities, accounts receivable, and notes receivable are not covered.

Records of accounts receivable. Although the standard fire policy does not cover fire losses on these records, they can be protected by a special agreement which insures against loss or damage to accounts receivable resulting from destruction of the accounts receivable ledger or records by fire or by other perils. These special agreements are not standardized.

Insurance which covers records of receivables usually provides that they be kept in a fireproof safe, vault, or cabinet when not in use. The policy may also require that a list of persons who owe the firm money be brought up-to-date periodically, and be deposited in a vault not on the premises of the store. Some forms of this coverage require that the total amount of accounts receivable be reported within ten days after the close of each month. The policy may cover accounts which are not over sixty days old or it may cover all accounts under one year old. Provision may or may not be made, in case of loss, for the deduction of an amount equal to the normal bad-debt loss of the insured. Installment as well as ordinary open-book accounts may be covered.

If the owner keeps his accounts receivable records in a fireproof vault or safe when not in use, there may be little need for this kind of insurance. Likewise, the policy may be unnecessary if his amount of credit business is small or done with carefully selected credit risks. Before obtaining this insurance the retailer should consider, in addition to the rate at which it is offered, the possibilities of damage to the records in case of a partial burnout, and the likelihood of a fast-burning fire of intense heat in which the records would be completely destroyed.

Merchandise. The stock of merchandise should be insured to the extent of its correct value. This value is not the invoice cost. All activities of a store are concerned directly or indirectly with the buying and selling of merchandise and even before a shipment of merchandise has arrived at the store it has cost the store more than the invoice price. In addition to transportation charges, buying costs have been incurred. Next come receiving, marking, and storage charges. The merchandise should also bear its share of the general administrative and other expenses. Some of these expenses have a direct and others have an indirect relation to the merchandise. Certain expenses will vary with the time the merchandise is in stock; others are not affected by the time element.

To determine the value of the goods on hand at a given time may not be an easy task, but the importance of doing it will be emphasized strongly following a loss by fire. If the insurance covered only the invoice cost of the merchandise, there may be a loss equivalent to the expenses incurred in connection with acquiring and holding the goods until the time of the loss. The extent to which the working capital has been impaired may be determined by comparing a balance sheet for the day before the fire with one prepared after the insurance company has made its settlement and the inventory has been replaced. Had no fire occurred, the expenses would have been recovered by the sale of the merchandise. An acceptable percentage should be determined which, when applied to the original cost, will give the proper insurable value of the inventory.

The standard fire policy provides for indemnification "to the

extent of the actual cash value (ascertained with proper deductions for depreciation) of the property at the time of loss or damage, but not exceeding the amount which it would cost to repair or replace the same with material of like kind and quality within a reasonable time after such loss or damage" and "without compensation for loss resulting from interruption of business." The "actual cash value" of the merchandise damaged or lost can be the invoice cost of similar merchandise at the time of the loss or during the "reasonable time" following the loss. It should be understood that this cash value can be more or less than what the retailer originally paid for his merchandise.

Another kind of policy furnishes provisional amounts of insurance depending upon the fluctuation in the value of the merchandise and fixtures. This coverage may be important to dealers whose inventories fluctuate widely from one season to another. Many retailers have large inventories in early spring and fall bought in anticipation of their peak selling seasons. Merchandise still on the manufacturer's premises but owned by the retailer is also covered by this insurance. A specific amount of insurance is provisionally established for each location and a portion of the premium calculated on this basis is deposited with the insurance company. At the end of the year, the payable premium is determined on the basis of the actual values; and settlement is then made in favor of either the merchant or the insurance company. To qualify for this kind of insurance the retailer must have merchandise, fixtures, and improvements of a value to justify a certain minimum premium. The policy rate is lower than one which applies to small stocks and equipment.

Furniture and fixtures. Furniture and fixtures are usually covered by the same policy which covers the building and merchandise. Sometimes they are covered in the same paragraph or clause. From the retailer's viewpoint this is undesirable. Because of the expenses incurred in preparing merchandise for sale, its investment value is increased after it is brought into the store. The value of furniture and fixtures, because of the wear and tear of use, is decreased after they are brought into the

store. Both the store and the insurance companies recognize this depreciation of furniture and fixtures, but the appreciation of the merchandise is less readily recognized. One of the main objects of sound underwriting is to reimburse the assured for the loss in value sustained. A form of insurance which covers furniture, fixtures, and merchandise in the same clause and in the event of loss recognizes depreciation of value for the first two but not the appreciation of value for the third does not accomplish this main object.

Building and equipment. The form which is to cover the building and fixtures should be examined closely to determine if it covers all the store equipment and in the manner desired. The form should contain the words "all permanent fixtures" or mention the equipment specifically.

The determination of the value of the building and equipment to be insured is often a difficult problem. Values of real estate change often. It is the object of fire insurance to indemnify the assured only to the extent of the loss sustained. In no event, however, will the amount of the indemnity exceed the face amount of the policy. Consequently, it is important to give the value of the building and its equipment careful consideration. Few fires result in a complete loss of the building and usually they do not injure the land.

Coinsurance

Most fires cause a partial loss only. Some property owners therefore carry insurance on only part of the property value. Thus, if a building valued at $100,000 is insured for $40,000 and a loss occurs up to $40,000, the owner collects the full amounts of the loss. Let us say that two buildings are each valued at $100,000; one owner, A, carries $30,000 insurance and the other, B, carries $100,000. Under the ordinary or standard policy, owner B's insurance premiums are three and one-third times as much as A's. Now suppose that a fire damages each building to the extent of $20,000; each owner will collect $20,000 from the insurance company. Since most fires cause only partial loss, it hardly seems fair that the two owners collect

the same amount when one paid three and one-third times the premium of the other. To avoid some of this inequality and induce property owners to carry more insurance, the companies introduced a clause which provides that, in case of loss, the company is liable for the same proportion of the loss that the amount insured bears to the actual value of the property. This is known as coinsurance (contribution clause, reduced rate average clause). By coinsurance we mean that the owner of the property bears part of the risk and so is a coinsurer with the insurance company. A common provision requires the assured to carry insurance to the extent of 80 per cent of the value of the property in order to collect the full amount of a partial loss. This is known as the 80-percent clause.

Now assume that A and B have buildings each valued at $100,000 and that they take coinsurance policies with the 80-percent clause: A for $30,000 and B for $80,000. Suppose that each building is damaged to the extent of $20,000; B will be paid the full $20,000, and A will be paid $\frac{3}{8}$ of $20,000, or $7,500. In case either insured has a total loss, he collects the face amount of his policy.

Under the 80-percent coinsurance clause for a $100,000 property, other situations are as follows:

INSURANCE CARRIED	LOSS	INSURANCE COMPANY PAYS	LOSS TO INSURED
$40,000	$ 50,000	$25,000	$25,000
60,000	50,000	37,500	12,500
60,000	80,000	60,000	20,000
80,000	80,000	80,000	0
80,000	100,000	80,000	20,000

The rate with a coinsurance clause is so much less than the standard fire rate without it, that every retailer should carefully consider the desirability of the coinsurance clause in his policies. To illustrate, a standard policy covering furniture and fixtures may cost $20.20 per $1,000 but the policy with the 80-percent coinsurance clause would cost only $7.16 per $1,000.

Business Interruption Insurance

The fire policy provides insurance only against loss or damage which is directly due to fire. During the period of business

interruption following a fire, expenses which have been incurred for future operations are not recovered but are lost. In addition, the expected profits are not earned. However, insurance is available to protect against this loss until normal operations can be resumed. This coverage, called use and occupancy insurance, or business interruption insurance, is practical when satisfactory accounting records are kept and modern planning or budgeting can be or is practiced. The basis for this insurance is a comprehensive work sheet indicating the estimated expenses and profit for the budget year.

The policy provides protection against either a total or partial suspension of business resulting from named causes. A form suitable for retailers provides protection *pro rata* on two items. The first item of protection is expenses which the retailer must continue to meet and the second is the lost profit. Item 1 covers the ordinary payroll for a period of ninety days. Expenses incurred by the store in reducing the amount of the loss are also covered. In the determination of the amount of expenses and net profit the policy provides that due consideration shall be given to the experience of the business before the fire and the probable experience thereafter. Because there is an important difference between the sales volume during the best month of the year and the worst month, this provision is important.

Another policy or contract indemnifies the insured on the basis of average daily profits which would have been earned during the period of business interruption. The limit of the company's liability or the limit to the amount which may be recovered by the retailer is 1/300 or other daily fraction of the amount insured. For those businesses which have important seasonal variations, a special form provides for increased protection during the more active period or periods. Because daily sales may vary widely during the week, a form is also available which provides insurance on a weekly basis rather than on a daily basis with recognition of seasonal variation.

Another form of coverage which may be desirable provides indemnity for the reduction in gross earnings minus the expenses which do not necessarily continue. Gross earnings are

defined as total net sales less cost of merchandise sold, plus other earnings derived from the operation of the business. The indemnity is provided for such length of time as would be required, with the exercise of due diligence and dispatch, to replace or repair the building. There is no daily or weekly limitation on the amount of the indemnity. The ninety-day limitation of liability is not placed on the ordinary payroll. For the latter, coinsurance is required and advantageous rates apply.

Additional expense insurance. If the building is destroyed by fire, the retailer may choose to continue operations at another location. The cost of moving to and from this other location as well as the cost of occupying the location may be insured by an additional-cost indemnity contract. This coverage may be adequate if there is little or no rent income to protect.

A policy is also available to cover expenses incurred in excess of those which would normally have been incurred had there been no fire.

Leasehold interest insurance. Should the building be leased rather than owned, the lease may contain a fire clause which permits the owner to cancel the lease in the event of a fire. This could result in a serious loss to the retailer if rents have risen since the lease was signed. The insurable interest of the store is the difference between the rental value of the premises at the time of the fire and the actual rent paid during the remainder of the term of the lease.

Improvements made to the premises by the lessee are an insurable interest. Upon the expiration or cancellation of the lease, improvements and betterments made to the property usually pass to the owner. It may be desirable to protect them against loss by fire as well as against loss by cancellation of the lease.

Tornado Insurance

Windstorm or tornado insurance covers direct loss or damage from wind. It also covers fire damage which is the result of windstorm if the fire policy ceases to operate because the build-

ing falls. The windstorm policy often includes damages from hail and this inclusion is required in many states. Windstorm damage is important in the Mississippi Valley, and along the Gulf and Atlantic Coasts. Earthquake insurance is important on the Pacific Coast.

Extended Coverage

Extended coverage policies are important. They provide insurance against direct loss from hazards not included in the standard fire contract. Hazards usually included are windstorm, hail, explosion, riot, civil commotion, smoke and vehicle damage. Common practice is to include fire protection and extended coverage in the same policy.

Life Insurance

Life insurance is usually taken to protect one's dependents. However, it is often desirable to carry life insurance on partners, owners, or important executives of a business payable to the business or to the surviving partner. The success of a business usually depends on the ability of its managers. If the success of a business depends primarily upon one man and this man dies, the business may suffer a heavy loss until he can be replaced. Insurance may provide the money to cover this loss and prevent the liquidation of the business. Perhaps two or more men are important to the continued successful operation of a business. It is more or less common practice to cover these men with life insurance payable to the business. Some important executives are so covered by policies running into hundreds of thousands of dollars.

Burglary, Robbery, and Theft Insurance

The merchant's property is subject to loss through criminal acts of others. Even though the criminal is apprehended and punished the retailer may not recover his property.

Burglary is defined as an act occasioned by any person or persons making felonious entry into the premises by actual force

and violence when such premises are not open for business and there shall be visible marks made by tools or explosives at the place of such entry. For an act to constitute burglary, then, forcible entry and visible marks of such entry must be made.

Robbery is the felonious and forcible taking of property by violence or the threat of violence to the person in custody of the property at the time. To constitute robbery, the property must be taken forcibly and violence must be committed or threatened.

Theft involves neither acts of force nor acts of violence but simply the felonious taking of the property of another. The term "theft" and "larceny" are used interchangeably.

Embezzlement is the fraudulent taking of the property of another while that property is in one's custody. Embezzlement differs from theft in that the thief has not had possession of the property prior to his criminal act.

Forgery is the false making or material alteration of some written instrument.

To protect cash and other personal property against wrongful acts committed by an employee or employees, the retailer may use an individual fidelity bond. The retailer is thus protected against the acts of a named individual. Large retailers may use a name schedule bond, a position schedule bond, or a primary commercial blanket bond. If a name schedule bond is used, the names of individual employees are listed. If a position schedule bond is used, protection is provided against the wrongful acts of any employee holding certain positions. The employees are not named but only positions are listed. The primary commercial blanket bond covers all employees and eliminates the necessity of making either a list of employees or positions.

For the small retailer, a package policy has been prepared to protect him from loss due to acts of burglary and robbery. The retailer is protected to the extent of $250 against seven different risks. These are robbery inside the premises, robbery outside the premises, kidnaping and stealing from custodian or messenger (e.g., on the way to the bank), burglary of money and securities from night depository or the retailer's residence, burglary of merchandise, safe burglary, and damage from burglars or

robbers. The limit on each unit is $250 on each of these seven hazards (or a total of $1,750), but the merchant may take more than one unit at reduced rates for the second and third units. Larger retailers need more than $1,750 (a typical maximum on the package policy), and so take regular burglary, robbery, and theft insurance.

Burglary, robbery, and theft are very real hazards, especially to retailers handling goods of high unit value such as jewelry, furs, coats, dresses, suits, and other types of clothing. A single truck or car can carry away several thousand dollars' worth of such goods. Not infrequently is a retailer forced into insolvency and out of business by a single burglary. A thief drives a truck back of the store, forces open a window and takes most of the retailer's coats, suits, or dresses. This deprives the retailer of the largest part of his inventory; and if most of his capital is invested in inventory, he may be unable to stand the loss. Yet the majority of retailers do not carry burglary insurance. They say it costs too much. One reason for the high cost is the number of inside jobs or jobs in which the store owner is in collusion with the burglars. Many commercial crimes of this type are detected and the perpetrators sent to prison, yet "phony" burglaries continue, especially in some of the garment trades.

If the merchant finds insurance too expensive, he should use especial care to have good locks on all doors and windows, to have rear doors and windows barred, and to see that the building is locked securely at night. Burglar alarms may be used, too. Merchants often coöperate to hire night watchmen to supplement the regular police force.

Whether or not the retailer finds burglary, robbery, and theft insurance on goods too expensive, he should carefully consider carrying sufficient insurance to cover the amount of cash which he usually has in the store.

Delivery Equipment

Delivery equipment may be destroyed or damaged by fire, collision, theft, flood, lightning, windstorm, or other causes.

Often of greater importance than these hazards is the danger that the owner will be liable for damages resulting from accidents. Damages may arise from property damage to other cars or from injury or death of persons. Not infrequently are such damages so large that the retailer is financially ruined by them. One may afford to assume the risk of loss to his delivery equipment, but it is rank folly not to carry liability insurance.

The combined automobile policy provides insurance against loss of, or theft of, or damage to, the vehicle, and liability for damage to others. The liability of the insurance company for loss is limited to the actual cash value at the time of the loss.

Policies are available covering all or any of the hazards mentioned, and the cost varies with the coverage. The cost may vary with the location of the business. Traffic hazards are higher in large cities than in small towns. Cost sometimes varies with the record of the insured for accidents and claims. It is generally considered good business to carry adequate liability insurance, and also insurance against fire and theft. Collision insurance (against damage caused to one's equipment by contact with other objects) is more expensive. Some retailers carry this risk themselves. However, deductible policies are available which greatly reduce the cost of collision insurance. Under such policies the owner bears the first part of a loss. Under a $50 deductible, the owner bears the first $50 loss and the insurance company pays damage over that amount.

Liability Insurance

In the conduct of his business a retailer may become liable to others owing to circumstances not related to the operation of the delivery equipment. This liability may arise from negligence on either the part of the retailer or his employees. The liability may be for either bodily injury or for damage to the property of others, or for both.

Whoever owns or uses real estate may become liable to others if such other persons are injured on the premises. A customer may stumble and fall in the store and suffer injury, a cornice or other piece of material may drop from the building and injure

a passer-by, or the customer may in other ways injure himself while in the store. A suit for damage may result.

Elevators are another source of bodily injury. The elevator may operate improperly or persons may be injured while entering or leaving the elevator. These accidents will occur despite the fact that elevator manufacturers are ever alert to make improvements in their product and in spite of the fact that elevators are inspected carefully by state or local inspectors.

Construction work attracts the attention of passers-by who may in some manner be injured while watching the workers. Customers or passers-by may be injured by falling building materials or by stumbling over materials. To obtain compensation for injuries, they are likely to bring legal action against the store as well as the contractor. Accidents of this nature are unusual, but when a serious one does occur, the merchant may face heavy damages. In such a case, the cost of insurance would be small by comparison.

If the dealer sends his men outside his store to install or repair appliances or other goods, he needs insurance to cover damages to property or persons resulting from their operations.

A customer may be injured by using a product purchased in a retail store. In some cases the retailer is held liable and in others the liability is held to be that of the manufacturer of the product. Injuries resulting from the use of a product are rare but they do occur. The consensus is that many damage suits for injury from manufactured products are in reality "blackmail"—that the complainant expects the defendant to settle out of court to avoid the unfavorable publicity resulting from a court trial. Some companies make a practice of settling such claims out of court but others, feeling that the suits are "blackmail," allow them to go to trial if the complainant persists in his efforts to collect damages. Some companies carry insurance against injury resulting from the use of their products, but such insurance is seldom carried by small retailers.

Workmen's Compensation

A retailer is liable not only for injuries which customers or others may suffer while in or near his store, but he is also liable

for injury to his employees. The various states have passed laws relating to this kind of insurance. Most of the laws provide the injured employee with medical benefits and compensation while disabled. In some states workmen's compensation insurance is compulsory while in others it is elective. In either situation, the retailer who is an employer is subject to a risk for which he should obtain insurance.

Rates

The cost of fire insurance varies widely with the location of the building, its construction, the condition of the building, the type of business, and the way the premises are kept. The fire rate on a fireproof building with sprinkler protection is a great deal less than on an ordinary frame building. A fireproof building surrounded by other fireproof buildings in a town with good fire protection will have a very low rate. The fire rates per $100 of insurance at one time for a typical store in two communities were as follows:

	TOWN WITH GOOD FIRE PROTECTION				VILLAGE
	Fireproof Building		Semi-Fireproof (brick) Building		Frame*
	Standard	80% Co-insurance	Standard	80% Co-insurance	Standard
Building	$0.192	$0.058	$0.70	$0.525	$1.60
Furniture, Fixtures and Merchandise	.432	.216	1.07	.91	1.60

* Coinsurance not available.

For extended coverage, rates on fireproof building were 0.28 cents standard and 0.016 with 80-percent coinsurance clause. On semi-fireproof or brick building the rate with 80-percent coinsurance was $0.96.

The advantages of fireproof buildings and the savings from coinsurance are obvious from this table.

Here is the insurance carried by one retailer who is located in a neighborhood business development in a city of over 100,000

population in a territory where tornado risk is small. The sales of this store were $45,000 and the average inventory was $15,000. We are not presenting this as an ideal insurance portfolio, but as the decision of one retailer at one time.

PROPERTY OR RISK INSURED		AMOUNT OF POLICY	ANNUAL PREMIUM
Burglary, robbery, and theft		$ 500	$ 45.00
Fire (goods and fixtures)		18,000	135.26
Public liability	Property	5,000	
	Personal	10,000	8.10
Automobile	Property	10,000	
	Personal	20,000	40.85
Total			$229.21

Buying Insurance

There are several other kinds of insurance that may be important. Plate glass insurance is important to stores with large display windows. Steam boiler and machinery policies may be needed by some large stores.

There is no general insurance against price changes but, as previously pointed out, many dealers hedge on the produce exchanges to prevent or limit loss from price changes.

The retailer obviously cannot afford to buy all the insurance available; to do so would mean probably that he operated at a loss. To make a wise decision he should consider the cost of the insurance, the likelihood of damage, and his own ability to guard against or lessen the danger of loss. He may reduce the risk of embezzlement by carefully checking on the character of all persons he hires. He can reduce the risk of burglary by locks, bars, alarms, night watchmen, and the like. He can reduce the danger of fire damage by using only fireproof buildings, installing automatic sprinkler systems on his property, and so forth. These reduce the insurance rate but do not eliminate the need of fire insurance.

Many retailers do not have the time to make a careful study of insurance. Too many insurance agents are "volume sales-

men" rather than expert counsellors. The merchant should try to find an agent who knows his business and gives honest advice as to the risks which should be covered. Such men (like all good salesmen) look at their jobs from the customer's point of view. They ask what insurance the retailer feels he needs, considering his type of business, his loction, his method of operation, and the character of his employees. Such agents are all too scarce; but if one can be found, he should be appreciated and patronized. Insurance should, of course, be taken only with reputable companies, of which there are many, both stock and mutual.

It is usually considered good business to carry fire and extended coverage on owned buildings, on merchandise, and on fixtures and equipment; automobile liability on all cars and trucks; public liability; and workmen's compensation. Other kinds of insurance should be carefully considered, especially burglary, business interruption, and life. Some dealers need contractor's liability insurance; others, plate glass insurance. The subject is too general to give specific information. What we want to emphasize is that insurance is important and that each and every business man should give it careful consideration. A large business often has one man who devotes all or a large part of his time to its insurance problems and policies.

Questions

1. Name the risks to which retailers may be exposed. Which risks are insurable?
2. What are three standards for determining whether or not to obtain insurance to cover a given risk?
3. Are records of accounts receivable covered by the standard fire policy?
4. If merchandise is insured for its invoice cost and a fire destroys it, will any loss be suffered by the retailer?
5. How should furniture and fixtures be covered?
6. If a store building valued at $20,000 is insured for $10,000 and the policy contains an 80-percent coinsurance clause, how much will the company pay the insured if a loss amounts to $6,000? To $10,000? To $12,000?
7. If a store building valued at $15,000 is insured for $12,000 and the policy contains an 80-percent coinsurance clause, how much

will the company pay the insured if a loss amounts to $4,000? To $14,000?

8. Why do insurance companies offer lower rates if the insured desires a coinsurance clause in his policy?
9. Should a retailer have the coinsurance clause in his policies?
10. Should a retailer, to build goodwill, distribute his insurance business among his customers who are insurance agents?
11. What loss will a retailer bear if his building is destroyed by fire and he does not have business interruption insurance?
12. What is leasehold interest insurance?
13. What is extended coverage insurance?
14. When should the retailer obtain life insurance?
15. Define the following: Burglary, robbery, theft, embezzlement, forgery. How may the small retailer protect himself against these hazards?
16. How should delivery equipment be insured?
17. What liability insurance should a retailer obtain?

33

Profits and Failures

WHOEVER owns and operates a retail store bears the risk of failure and loss of his capital. He may earn large profits. Some retailers seem neither to fail nor succeed. Many earn less than an employee and spend their time hoping business will get better. There are many explanations of successes and failures. Normally, however, when the sales of a store are increased, the profits are increased.

Increasing Sales

Sales can be increased by carrying merchandise which is in demand, informing consumers that desired goods are in stock, and operating a store that is attractive to consumers.

Having what people want. In a survey of a trading-center town it was found that this town had increased its trading area during the past decade. Why did more people from the competitive borderline territory come to this town to trade? When asked their reasons, these people repeatedly mentioned two stores which carried large stocks at attractive prices. In other words, people could find what they wanted in these stores—merchandise in the sizes and colors desired, and at the right prices.

People visit a store where they expect to find what they want. A store whose theme song is, "We don't carry it," or "Sorry, we are out of stock," is a store that is driving its customers away. A retailer should select lines which suit community needs, competitive conditions, his available capital, and his own interest and aptitude for handling and servicing various lines.

Practically all people wish to buy at reasonable prices, and some are definitely price-conscious. A retailer who does not wish to have the reputation of being "high-priced" may be able to use leaders effectively to establish a reputation for having low or reasonable prices.

Letting people know what you have. Too many retailers assume that the public knows what they have to sell. Actually, consumers can only find out by being told or by visiting the store. Consumers want to know what a store has for sale and at "what price." The retailer can tell the people in his territory what he has to sell, and what the price is, by using window displays, advertising, and other methods.

An attractive and friendly store. Consumers are drawn to an attractive store, a clean store, a store with good displays, and, especially, to a friendly store. Two stores were located in the same block. Their stocks and prices were about the same; both used open displays. A was more firmly established in the community, had better window and inside displays than B, kept his store cleaner and his stock more attractively arranged. Yet B outgrew him. B was friendly. He knew most of his customers by name; he had a friendly word for each of them. A was more "businesslike"; he waited on consumers courteously, wrapped their packages, made change, but that was all. B added something of his personality; that little "extra" in a friendly word or smile. Both were good stores, both fairly profitable stores, but gradually B outgrew A. As his sales increased so did his stock and he came to have the advantage of a more complete stock. This came partly from more attention to stockkeeping and buying, and more searching for the goods his customers wanted.

Additional lines. Some retailers increase their sales by adding additional lines. Local demands, competitive conditions, and the ability of the retailer to sell and service the goods should be considered if the retailer adopts this plan. The dealer may believe that there is an opening in his territory for a new line of merchandise. He may find that no local store handles an adequate line of the goods. If he really wants to develop a worthwhile business in the new line, he should first be thor-

oughly familiar with it and interested in it; otherwise, he should employ a competent salesman.

Plans for store expansion frequently include the addition of new products or lines. The retailer who intends to increase the variety of his merchandise should select those lines which are in demand in his community, and should plan to carry a reasonably full and complete stock. If he carries a little of many lines he will have an unattractive store; furthermore, no line will be complete.

Increasing Profits

A firm seeks to increase its profits by stepping up sales. There are, however, other ways of increasing profits. Since profit is the difference between a retailer's gross margin and his expenses, he may increase his profit by increasing his margin or decreasing his expenses.

A retailer buys an article for 75 cents and sells it for $1.00. He has a margin of 25 cents. This margin may be increased by buying the article at a lower price or selling it higher. If he can buy the article at 70 cents and sell it or $1.00, he has a margin of 30 cents. If he buys it for 75 cents and sells it for $1.05, he has a margin of 30 cents. If he pays 70 cents and sells for $1.05, he has a margin of 35 cents.

Higher prices may be obtainable on some articles, or by dealers in locations with little competition, or from high-income customers. The retailer who tries to raise his prices, however, may see his sales decline. Higher prices do not offer a practical way of increasing margins for many retailers.

Lower buying prices offer greater promise of increasing margins. Many wholesalers are trying to reduce the expense of getting goods from the manufacturer to the retailer. These plans, however, arise chiefly from the belief that it is necessary for the retailer to buy at lower prices in order to meet the prices of the chain stores. Therefore, the lower cost prices will presumably be passed on to the consumers and not retained as higher margins by the retailers.

The retailer himself can devote more attention to buying and

so reduce his cost prices on some goods. He buys certain items direct from manufacturers and has them drop shipped, or sent in pooled or collective cars. Sometimes he can pool his order with those of other retailers through buying clubs and so obtain lower prices; or he can buy job lots or surplus goods. In any of these cases he must be careful to avoid overbuying or buying unsalable goods.

Another way of securing lower prices is to buy from local or nearby factories so that delivery expenses will be low. Small manufacturers will often sell at somewhat lower prices than large manufacturers whose brands are widely advertised. The wholesalers also may have their own private brands at prices somewhat lower than the nationally known brands. In some instances retailers have sold these relatively unknown brands profitably and have made them well known in their territories. The relative merits of widely advertised brands and little advertised brands have been discussed earlier (see pages 109, 310). We will only repeat here that there is no one best policy that fits the needs of all retailers. Each retailer should consider his local situation, the merits of the specific brands available, and his own ability to sell them.

Some dealers increase their average margin by adding higher-margin lines. One such dealer went to an experienced electrical appliance retailer and said that he wanted to sell the larger electrical appliances because of their high margin. The experienced retailer told him that he could not expect to make a success of selling electrical appliances unless he was prepared to service them. Although these appliances carry a wide margin, they are not necessarily more profitable. High-margin lines may appear attractive, but the retailer must consider his expenses before he concludes that they will yield a high profit.

The surest way of increasing profits is to decrease expenses relative to sales. A retailer with unsatisfactory profits may retain the same sales volume and reduce his actual dollar expenses. The savings will increase his profits. He may keep his actual dollar expenses constant and increase his sales. Or he may increase his sales faster than he does his expenses. It may be easier to reduce expenses than to increase sales, however.

Variations in Expenses

The reported operating expenses of similar stores vary widely. For example, there were two stores located in the same state and they had approximately the same sales volume during the year. One reported expenses which were more than double those of the other: 27 per cent against 13 per cent. The first dealer, with 27 per cent expenses, did not include his salary in the operating costs; the 13-percent figure, however, included a salary for the owner.

During the year two retailers located in the same town had approximately equal dollar expenses. They paid the same rent, charged off practically the same amount of depreciation, and paid the same insurance—facts which suggest that they had equally good locations, equally good fixtures, and stocks of about the same size. Yet one retailer sold twice as much as the other and so his expense percentage was less than half that of his competitor: 9 per cent compared with 20 per cent. If we assume that both stores had margins of 18 per cent and that the first store had sales of $88,800 and the second of $40,000, their operations for the year were:

	A	B
Sales	$88,800	$40,000
Margins (if 18%)	15,984	7,200
Expenses	8,000	8,000
Profit or loss	$ 7,984 (profit)	$ 800 (loss)

A made a profit of almost $8,000 (over his salary) while B lost $800 (failed by $800 to earn his salary.) This is not an unusual example. Cases like it exist in every trade, in every industry, and in almost every town. Some merchants make money, some lose money, and many "just make a living." Most of those that earn a profit have low expense percentages.

Causes of variation in the expenses of retailers. Several factors cause the expenses of retailers to vary: the kind of merchandise handled, the services rendered to customers, the fluctuations in price level, the volume of sales, the size of the city, and the merchandising efficiency of retailers.

The kind of merchandise sold. It costs more to sell drugs

than to sell groceries, and it costs more to sell furniture than drugs. The expenses vary with the time and effort required to make sales, with the size of the individual sales, with the space occupied by the goods, with the services rendered, and with the rate of stock turnover. Because groceries are convenience goods, people ordinarily do not shop for them, that is, it is not necessary for salespeople to wait while customers make up their minds as to what they want. The grocer has a relatively high rate of stock turnover.

The drug store also handles convenience goods to a very large extent, but the great variety of goods which the druggist must carry slows up his rate of turnover. Goods sold at the soda fountain and in the prescription department require personal service. For these reasons the druggist has higher expenses than the grocer.

The furniture merchant sells in large units, but his merchandise is bulky and requires a large amount of space, thus increasing his expenses. People shop for furniture, which means that the salesman must show furniture to many people who make no purchases, thus creating periods when the salesman is idle. This time element adds to the selling expenses. Sales are likewise irregular. The quantity of goods required for a complete stock, and the seasonal nature of the business both slow up the rate of stock turnover and increase expenses.

Table 33–1

GROSS MARGINS AND OPERATING COST IN 50 RETAIL TRADES, 1939

(Medium averages of figures for all stores, both profitable and unprofitable, expressed as percentages of net sales; trades listed in order of gross margin percentages.)

TRADE	GROSS MARGIN	TOTAL EXPENSE
Custom Tailors	63.2	61.9
Monuments	62.1	59.1
Florists and Nurseries	58.4	53.3
Bakery Shops	54.0	48.0
Furs	50.2	44.6
Garages	48.9	46.8
Jewelry	48.9	43.6
Radios	44.5	42.1
Restaurants, Eating Places	43.3	39.2
Gifts, Novelties, and Souvenirs	42.3	36.0

TABLE 33–1—Continued

TRADE	GROSS MARGIN	TOTAL EXPENSE
Furniture and Undertaking	42.1	37.5
Office Equipment and Supplies	40.4	37.4
Musical Instruments	39.7	37.6
House Furnishings	39.4	37.2
Dairy and Poultry Products	39.2	35.5
Furniture	38.1	33.7
Floor Coverings	37.0	34.7
Drinking Places, Taverns, Bars	35.9	31.9
Lingerie, Hosiery, Millinery, etc.	35.8	32.5
Books	35.4	34.8
Electric and Gas Household Appliances	35.3	32.8
Paint, Wallpaper, and Glass	34.9	32.7
Automotive Accessories and Parts	34.3	29.1
Men's Furnishings	34.2	33.2
Confectionery	34.1	29.3
Sporting Goods	33.2	30.5
Stationery	33.0	30.0
Shoes	32.9	30.7
Men's Clothing	31.8	28.3
Limited-Price Variety	31.5	26.5
Family Clothing	30.6	27.3
Women's Ready-to-Wear	30.5	28.7
Drugs	30.5	28.1
Coal and Other Fuel	30.1	27.3
Hardware and Furniture	29.9	26.9
Hardware	29.1	26.7
Dry Goods, General Merchandise	28.1	25.1
Lumber and Building Materials	26.9	24.0
Alcoholic Beverages	26.8	24.2
Filling Stations	24.3	22.3
Cigar Stores and Stands	23.9	21.6
Meats	23.5	21.7
Hardware and Farm Implements	20.4	20.6
Farm Implements	19.7	18.7
Groceries and Meats	19.2	17.3
Groceries	18.4	16.9
Country General Stores	17.9	15.4
Farmers' Supplies	17.5	15.0
Motor Vehicles	17.1	15.9
Groceries with Filling Station	16.8	15.7

Source: *Standard Ratios For Retailing* by W. L. Mitchell, Jr. New York: Dun & Bradstreet, Inc., 1941.

Retail establishments, such as jewelry, radio, plumbing, and electric shops, garages, and restaurants, that repair or make goods have higher expenses owing to the extra amount of labor required.

Services rendered. The services rendered customers affect the dealer's expense. The store that extends liberal credit and makes deliveries has higher expenses than the store operating on a cash-carry basis, other things being equal. The self-service store usually has lower expenses than the store employing salesmen. The store equipped with expensive fixtures, rest rooms and writing rooms and with a liberal policy on returned goods will ordinarily have higher expenses than a store giving less service.

According to estimates, it costs retail grocery and hardware stores from 5 to 8 per cent for credit and delivery service on goods sold on that basis. The cost of credit includes the interest on outstanding accounts; the losses from bad debts; the labor in keeping books; and the cost of making collections—sending out statements and collection letters, the use of personal collectors, lawyers, and collection agencies. Few stores, however, do all of their business on credit, and very few deliver all their goods. For these reasons, the cost of credit and delivery service to most grocery and hardware stores is less than 5 per cent when computed on total sales.

Fluctuations in the price level. The relative or percentage cost of operating a store declines when the price level advances, and increases when the price level declines. The reason is that operating expenses advance or decline less rapidly than the prices of the goods themselves.

More than one-half the expense of operating a retail store is composed of salaries and wages. It is well known that advances in salaries and wages lag behind advances in the prices of commodities. Rent is approximately one-sixth the expense of retailing; and since retailers frequently lease their store buildings for a period of several years, rent also lags behind prices. Taxes do not move with commodity prices. Insurance rates likewise are slow to change and in any event are not increased until the expiration of policies, which may be for periods as long

as five years. Newspaper advertising rates do not change as fast as commodity prices. A retailer may increase his store space when prices are rising and decrease it when prices are falling, but the percentage cost usually changes very little. The costs of electricity, water, and telephone service do not fluctuate with every change in the price level. The same is true of freight rates and interest rates. Over short periods, depreciation charges are not changed. Losses due to bad debts are likely to decrease in periods of rising prices and increase in periods of falling prices. About the only other expenses which increase significantly when commodity prices rise are those expenditures which must be made for the commodities which are increasing in price. These may be such as wrapping materials, gasoline, coal, and other miscellaneous commodities. These make up but a small part of a retailer's expenses.

Another factor which helps to lower the relative cost of doing business in a period of rising prices is the increased prices which the retailer can obtain for merchandise purchased previous to a wholesale price rise. This increases the sales without an increase in the cost of goods sold. There may be a slight increase in the dollar amount of expenses before the merchandise is sold but over-all total expenses tend to decline.

The volume of sales and expenses. In periods of rising prices more people are employed and a retailer can increase the volume of his sales in terms of physical units. Those expenses which increase but slowly are reduced per physical unit of merchandise sold. Normally a retailer can handle a considerable increase in his inventory—the number of pounds, yards, or gallons—without expanding his space facilities. Those of his expenses which are of a fixed nature decline per unit as the number of units sold increases.

Stores with a large sales volume, conducting business in the same manner and in the same- or similar-sized cities, do business at a relatively lower cost than do stores with a smaller volume. The reason is that basically retailing is the performance of the buying and selling functions, and the amount of merchandise bought and sold can be increased considerably with no important increase in expenses. An elevenfold increase in the sales

volume of a store would not necessarily require expenses to be increased by eleven times.

To attain a desired volume of business it may be necessary to reorganize the store's operating methods or move to a larger city. Under such conditions, expenses may increase at a faster rate than sales. If the retailer, in order to expand, chooses to perform wholesaler services in addition to his regular retail functions, then expenses may increase more rapidly than sales. In larger cities expenses are normally higher than in smaller cities for reasons which will be shown.

Although expenses may increase relatively as sales volume enlarges, this is not necessarily a reason to avoid increasing the sales volume. For example, a store may have a sales volume

TABLE 33–2

THE INFLUENCE OF SIZE OF COMMUNITY AND SIZE OF STORE ON OPERATING AND MERCHANDISING RATIOS, 1939

(Percentages of net sales)

	ANNUAL SALES VOLUME					
Population	Less than $10,000	$10,000–$20,000	$20,000–$30,000	$30,000–$50,000	$50,000–$100,000	$100,000–$300,000
			GROSS MARGIN			
Less than 20,000....	34.0	33.3	33.3	32.9	32.5	33.0
20,000 to 100,000...	36.6	36.7	36.5	35.3	34.6	34.5
100,000 to 500,000...	36.9	36.7	35.9	35.5	35.5	35.6
Over 500,000.	36.9	36.8	35.9	35.4	35.4	35.6
			TOTAL EXPENSES			
Less than 20,000....	31.4	29.4	29.4	28.7	28.5	29.5
20,000 to 100,000...	34.4	34.1	33.5	32.3	31.9	31.8
100,000 to 500,000...	33.8	33.7	33.1	32.8	32.1	32.3
Over 500,000.	33.9	33.8	33.0	32.7	32.0	32.3
			WAGE EXPENSE			
Less than 20,000....	5.9	7.2	8.4	9.3	10.4	11.2
20,000 to 100,000...	8.6	8.6	10.0	10.4	11.8	12.2
100,000 to 500,000...	7.8	7.9	9.9	10.9	11.8	12.0
Over 500,000.	8.0	8.0	9.7	10.6	11.5	12.0

Table 33-2—Continued

Population	Less than $10,000	$10,000–$20,000	$20,000–$30,000	$30,000–$50,000	$50,000–$100,000	$100,000–$300,000
			ANNUAL SALES VOLUME			
			SALARY EXPENSE			
Less than 20,000....	15.5	12.8	10.7	9.2	7.3	6.7
20,000 to 100,000...	13.3	13.2	11.1	10.0	7.4	6.9
100,000 to 500,000...	13.6	13.5	11.1	9.9	7.8	7.0
Over 500,000.	13.6	13.5	11.2	10.0	7.9	7.0
			WAGES AND SALARY EXPENSE			
Less than 20,000....	21.4	20.0	19.1	18.5	17.7	17.9
20,000 to 100,000...	21.9	21.8	21.1	20.4	19.2	19.1
100,000 to 500,000...	21.4	21.4	21.0	20.8	19.6	19.0
Over 500,000.	21.6	21.5	20.9	20.6	19.4	19.0
			OCCUPANCY EXPENSE			
Less than 20,000	6.0	5.0	4.3	3.9	3.6	3.6
20,000 to 100,000...	6.4	6.2	5.7	5.2	4.8	4.4
100,000 to 500,000...	6.8	6.6	5.6	5.2	4.7	4.6
Over 500,000.	6.7	6.6	5.6	5.2	4.7	4.6
			ADVERTISING EXPENSE			
Less than 20,000....	0.8	0.9	0.9	1.1	1.1	1.1
20,000 to 100,000...	1.0	1.0	1.1	1.1	1.3	1.4
100,000 to 500,000...	0.9	0.9	0.9	0.9	1.1	1.3
Over 500,000.	0.8	0.9	0.9	0.9	1.1	1.3
			BAD-DEBT LOSSES			
Less than 20,000....	0.7	0.5	0.5	0.5	0.5	0.5
20,000 to 100,000...	0.6	0.7	0.6	0.5	0.5	0.5
100,000 to 500,000...	0.7	0.7	0.4	0.4	*	*
Over 500,000.	0.6	0.6	0.4	0.4	*	*

*Not available.

Source: *Standard Ratios For Retailing*, by W. L. Mitchell, Jr. New York: Dun & Bradstreet, Inc., 1941.

of $150,000, expenses of 30 per cent, and a net profit of 5 per cent. The sales volume may be increased to $300,000 while

expenses increase to 32 per cent and net profit declines to 3 per cent. In the first instance the dollar net profit is $7,500 and in the second it is $9,000.

The size of the city. Expenses usually increase as the size of the city increases. Wages and salaries are generally higher in the larger cities than in smaller cities and towns because the cost of living is greater. Because the sales volume per employee does not increase as fast as the wages and salaries, the retailer's expense increases relatively.

Other expenses are also greater. The occupancy costs (all expenses connected with occupying a building) are greater in larger towns and cities. Land in a small town is worth but little more as a business site than it is for farming purposes. The cost of erecting and maintaining a building is less. The cost of government (taxes) is greater in larger towns because more municipal services are furnished, and the cost of performing them is greater. Delivery expense is greater because of the longer average distances of delivery routes. None of these expenses would increase if the sales productivity of a store could be increased as fast as expenses increase.

Failure

Many retailers cease operations every year. Some of them, when judged by any reasonable standard, have failed although the majority do not become bankrupt. Rare is the failure which occurs without the retailer and others having advance notice. Failure is not something which occurs with the unexpectedness of a sudden explosion; rather, it is a process which extends over a period of time. It may have set in at the very inception of the business. The business may have been foredoomed. In any case, signs of failure can be observed well in advance by the retailer himself or by a competent observer.

Many reasons are cited as the cause of failure, but usually no one thing is responsible. The retailer who fails is likely to be generally inefficient, and although he may cite one cause for it, observation and questioning will reveal other causes.

A common explanation given for failure is lack of capital,

but the retailer who offers this explanation might fail if he were given several times the capital which he considers necessary in order to succeed. His failure would only be postponed because of the longer time it would require to dissipate the larger amount. To achieve a given sales volume a certain minimum capital is required, but of two retailers with identical amounts of capital, one will fail and the other will succeed.

Lack of experience is also offered as a cause of failure. Two years' experience as a retail salesman is not necessarily an adequate qualification for the successful operation of a store. Some people with less have succeeded, and some with twenty years' experience have failed. Experience, however, in the different phases of retailing will reduce the possibility of failure. It need not necessarily be a long period of years but it should be more than experience as a salesman.

Poor buying, another cause of failure, is probably responsible for a larger percentage of failures than is commonly supposed. Examination of the inventory in a store that has failed will reveal many buying errors. The merchandise is not suitable for the customers to whom the store was catering. The assortments are very poor. Too much of some merchandise and not enough of other kinds were bought. The cost prices paid were too high. The successful retailer usually recognizes that the inventory of an unsuccessful retailer is no bargain. It is a conglomeration of buying errors. Merchandise which is "well-bought is well-sold."

A poor location also ranks high among the causes of failure. A well-located store is situated where an adequate number of customers will find it. A location selected because the rent is low can be an expensive location.

The lack of adequate records is important perhaps not as a cause of failure but certainly as a basis of failure. Too many retailers are unfamiliar with the elementary principles of double-entry bookkeeping. If a retailer has no knowledge of accounting principles, the time and money spent in acquiring the knowledge will be a very profitable investment. The lack of records of itself is not the cause of failure. It is the lack of information which these records provide which can be the cause

of failure. With adequate information, a person of average intelligence can make sound decisions. Without such information, a retailer makes assumptions about his operations which are not necessarily true.

Conditions which are beyond the control of the retailer may be responsible for failure. One of these conditions is declining prices. Every important decline in the price level is accompanied by an increase in the number of business failures. Merchandise can not be sold for what it originally cost. However, the most elementary fact known about prices is that they rise and decline. Though it is difficult to anticipate when a rise or a decline will occur, many retailers do so. These are the efficient retailers. By studying all the available facts they are able to assess correctly current conditions and to anticipate future prices. Declining prices and a shrinking demand do not cause them to fail. The condition is anticipated and preparation is made to meet it.

At times some alarm has been evidenced at the so-called high rate of mortality among retailers. It has been pointed out that the failure of a retailer is an economic waste. The effort of the retailer would have been more productive had it been directed into other channels. It has been suggested that steps be taken to reduce this waste by regulating the number who become retailers. Of course, effort which results in failure, on the surface at least, is wasted effort. Perhaps it may be a part of the price which must be paid to have a free and competitive business world.

Questions

1. What are some basic policies which will increase sales and thus contribute to the success of a store?
2. What are two basic methods of increasing profits? Under what circumstances is one likely to be more practical than the other?
3. How may gross margin be increased?
4. What are the causes of variations in expenses of retailers?
5. Illustrate and explain why it is more expensive to sell one kind of merchandise than another.
6. Illustrate how fluctuations in the price level affect a retailer's expenses.

7. When prices are stable, will expenses necessarily decrease as the sales of a store increase?
8. Why are the expenses of retailers located in large cities greater than the expenses of retailers located in smaller places?
9. What are the causes of retail store failures?
10. What are your recommendations for reducing the rate of retail store failures?
11. It has been proposed to have prospective retailers take an examination before they enter business. Should this examination be compulsory or voluntary? In either case, what should the examination cover?

IV. *The Control of Marketing*

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The Regulation of Competition

RELATIONS between business men and business organizations must be regulated, otherwise the law of the jungle would prevail. The regulation of business relations is just as necessary as is the regulation of social relations.

Ever since its beginning, organized commerce has been regulated in some manner. It is easy, however, to obtain the impression that business regulation is something very recent or that regulation is more strict and complete than formerly. Neither impression is wholly true. Most of our regulatory laws are refinements of laws which have existed for hundreds of years. In this chapter, the major statutes which regulate competitive relations will be discussed.

Sherman Act

The Sherman Act became a law July 2, 1890. At that time business organizations were increasing in size at a rapid rate and were frequently using methods that were contrary to the best public interest. Smaller competitors were crushed ruthlessly. Monopoly prices were often established. Competition was stifled. The attention of the public was attracted to the competitive wars going on in various industries and the belief became widespread that no general good was resulting from this strife in the business world. Various interests pointed out how they and the public were suffering real injury. There was a cry for Congress to put a stop to the vicious and injurious com-

petition between business rivals. The Sherman Act was the result. The power of Congress to pass such a law was based on the commerce clause of the Constitution which says that Congress shall have the power "To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes; . . ."

The Sherman Act was brief and to the point. It contained but eight short sections the first of which provided that "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations is hereby declared to be illegal: . . . Every person who shall make any such contract or engage in any such combination or conspiracy hereby declared to be illegal shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding $5,000 or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court." It was further provided that any person injured by a violator of the Act could recover threefold the damages sustained plus costs of the suit and a reasonable attorney fee.

Of fundamental importance is the fact that the power of the Sherman Act is the power to regulate only interstate trade. Business or trade which is conducted entirely within the boundaries of a state is *intrastate* trade. It is a subject of regulation for the particular state. The Constitution does not give Congress the power to regulate intrastate trade. Because this point is fundamental, the courts have often been called on to define and determine what constitutes interstate commerce. There has been an inclination to interpret the term broadly. All that is necessary is to have commercial relations or contacts extending across state boundaries which result in a sale and purchase, and everything which helps bring about the exchange has been held to be a part of interstate commerce. A defense plea that interstate commerce was not involved may be a weak one since in one manner or another a firm is likely to have relations extending beyond the home state boundaries.

The good motives or beneficial results which may result from some action are not a defense if the Act has been violated. If

competition or commerce has been restrained, it is no defense to plead the good results which may have come to the public from such restraint. If the Act has been violated, the penalties apply.

When the Act was first passed, there was a tendency for the courts to apply the law literally. In the cases against the Standard Oil Company and the American Tobacco Company in 1911, however, the rule of reason was laid down. Prior to that time, the penalties were to apply, no matter how small the violation of the Act. After the decisions of 1911, reason was to rule in interpreting the Act. Not every contract which restrained competition or trade or fostered monopoly was to be held a violation subject to the penalties of the Act. Only an unreasonable restraint of trade would be held to be a violation.

Whether or not a restraint of trade is unreasonable depends upon the facts of the particular case. The amount of the trade restrained is not necessarily a test of reasonableness. If the restraint of trade is absolute and direct, there is a violation of the Act although the amounts involved are small. Whether or not the prices fixed by business firms are of themselves reasonable is not a sound basis for invoking the rule of reason.

Restraint of trade may be direct or it may be indirect. An indirect and remote restraint of trade is not a violation of the Act. Whether or not the restraint is direct or indirect and remote again depends upon the facts.

Section two of the Act prohibits attempts to monopolize and combinations and conspiracies to monopolize any part of the trade or commerce of the several States, or with foreign nations. Not every monopoly, however, has been held to be a violation of the Act. The size of a business organization does not necessarily make it a monopoly nor does the integration of noncompetitive business units necessarily result in a combination which is in violation of the Act. A large business may or may not restrain trade and competition.

Combinations to prevent or restrict the flow of merchandise through a trade channel are violations of the Act. Examples are (1) when retailers combine to prevent manufacturers and wholesale merchants from selling direct to consumers and (2)

when wholesale merchants combine to prevent manufacturers from selling directly to retailers. The Act, however, does not prevent an individual seller from choosing the customer to whom he sells unless it can be established that such a seller has a monopoly.

Price Discrimination

To amplify and extend the Sherman Act, the Clayton Act was passed October 15, 1914. Section two of this Act legislated against price discrimination. For twenty-two years the section remained as originally passed. On June 19, 1936 the section was amended by the Robinson-Patman Amendment. The primary object of the Amendment was to prevent chain stores and other large purchasers from obtaining more advantageous prices and other benefits than other purchasers.

The Amendment, like the original Act, prohibits price discriminations, but it does not prevent a seller from giving one buyer a lower price than another. It is possible to give one buyer a lower price than another buyer if the following conditions prevail:

1. The article sold to buyer A is of a lower grade or quality than that sold to buyer B.

2. The granting of the lower price does not substantially lessen or prevent competition.

3. The lower price granted to a given buyer is due to a lower cost of manufacturing his goods than the cost of manufacturing goods sold to other buyers. Many conditions can cause the cost of manufacturing to vary.

4. The lower price given to one buyer is due to a lower cost of selling to one than to the other.

5. The lower price given to one buyer is due to a lower cost of delivering to one than to the other.

6. The lower price granted to one buyer is due to changing market conditions.

7. The lower price granted to one buyer is due to a service granted proportionally to all competing buyers. In other words,

the granting of an advertising allowance has the effect of granting a lower price, but as long as it is granted on a proportional basis no discrimination is involved.

The Amendment does not make any type of discount valid or invalid of itself. The validity of any discount is dependent upon numerous factors. The Amendment provides the general guides for testing the validity of any particular kind of discount. Consequently, a given type of discount is legal under proper conditions and illegal under other conditions.

Resale Price Maintenance

The ability of advertising to create goodwill for the manufacturer of a branded or easily identifiable article has long been recognized. Branded merchandise which has been highly advertised will usually have a higher rate of sale. This circumstance makes nationally advertised merchandise desirable as loss leaders. For a long time retailers had considerable freedom in using as leaders whatever nationally advertised merchandise they wanted to use. They often used nationally advertised brands. Smaller retailers were often undersold and they objected. An appeal was made to manufacturers on the basis that the manufacturer's goodwill was injured by the promiscuous cutting of established prices. It was pointed out that the consumer thought less of a product which he could buy at a considerable reduction from the customary price. The validity of this argument is still hotly debated. By 1931, however, the proponents of resale price maintenance had sufficient strength to obtain the passage in California of the first of the so-called "Fair Trade Laws" or Resale Price Maintenance Laws. By 1945 all states except Missouri, Texas, and Vermont had passed similar laws.

The State laws made legal a contract whereby an owner or distributor of a branded product specified that the product must be resold at certain prices or above certain prices. Until 1937 such contracts, if interstate commerce was involved, were in violation of the Sherman Act. In that year, however, the Sher-

man Act was so amended by the Miller-Tydings Amendment that contracts drawn according to the State "Fair Trade Laws" were no longer illegal in interstate commerce.

It must be understood clearly that the Resale Price Maintenance Laws, or so-called "Fair Trade Laws," legalize only vertical price fixing; horizontal price fixing is not affected. In other words, a resale price-maintenance agreement can be made only between organizations which belong to different stages of a trade channel. It is legal for a manufacturer to agree with a wholesale merchant or with a retail merchant that the wholesale merchant or the retail merchant will sell at or above certain prices. The same applies also to wholesale and retail merchants. Price agreements made between members in the same stage of distribution (competitors) are horizontal price agreements and they are contrary to the Sherman Act.

It is to be observed, however, that a manufacturer, insofar as his own product is concerned, can in effect use horizontal price fixing by requiring all wholesalers who handle his product to maintain the resale price of it. He can make the same requirement of all retailers.

To be eligible for a resale price-maintenance agreement a commodity must meet two requirements. It must bear a trademark, brand, or name of the producer or owner of the product. The product must also be in free and open competition. The object of this is to prevent a monopolist from acquiring the privilege of maintaining resale prices.

In twenty-four states it is not necessary to be the owner of the trademark or the brand name in order to establish the resale price of a commodity. All that is necessary is to become an owner of the product which bears the brand or trademark. Such a person can establish resale prices for a branded commodity without regard to the wishes of the brand's or trademark's owner. If the latter objected to such action, he could shut off the supply of the product to the offending wholesaler or retailer.

In twenty-nine states contracts establishing the minimum resale prices of products are made legal, while in sixteen states contracts which establish specific or *absolute* prices are legal.

A wholesaler or retailer located in one of the first group of states would have some latitude in adjusting prices to the requirements of the local market. No such adjustment would be possible in the second group.

A most significant provision of all State "Fair Trade Laws" is that it is not necessary to be a party to a resale price-maintenance contract in order to be bound by the provisions of the contract. All that is necessary is to give notice to a wholesaler or retailer that the particular product is subject to a Fair Trade Act and such dealer is bound to comply with the provisions of the contract. The notice may be given by attaching a sticker to the product or to the invoice, or by sending the dealer a copy of the contract.

From time to time merchandise which has been the subject of a Fair Trade contract is obtained by dealers but it no longer bears the trademark or brand of the producer, and the merchandise is not otherwise easily identified as the product of any particular manufacturer. In some states such merchandise can be sold at less than the Fair Trade prices on the theory that the goodwill associated with the brand or trademark (no longer attached to the product) can not be injured by selling the product at a reduced price. A dealer selling such a product, however, must not refer to the brand in any way. Some states also have laws prohibiting the removal or obliteration of brands or trademarks.

A dealer may sell below the established prices if he is in good faith closing out a line. Some states, however, require that the owner or distributor of the product be given an opportunity to repurchase the product. A dealer who previously has never handled a product that is subject to a Fair Trade contract, and who proceeds to sell the product below established prices can not be said to be closing out a line.

When merchandise deteriorates or becomes damaged, it may be sold in all states without regard to established prices if notice is given to the public of such damage or deterioration. Likewise, merchandise sold at the order of the court is exempt from these provisions of the Acts in all states except Wisconsin.

Price Floor Laws. More than one-half of the states have laws

prohibiting sales below cost, or below cost plus a minimum markup—often specified as 6 per cent over invoice cost. These laws are intended to prevent the use of "loss leaders," which are regarded as an unfair method of competition. Exceptions are made when a product is damaged or when it must be sold quickly to prevent spoiling, or when the price is reduced to meet competition. These laws are of doubtful constitutionality in some states and difficult to enforce in all of them. The small retailer is not likely to be bothered by these laws unless he makes frequent use of cut-price leaders.

The Federal Trade Commission

On September 26, 1914 the Federal Trade Commission Act was passed. This Act established an organization and procedure for handling unfair and allegedly unfair methods of competition. The Act itself does not indicate what are unfair methods of competition but states that "Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are hereby declared unlawful."

The Commission consists of five members appointed by the President with the consent of the Senate. It has the power to investigate whatever may appear to be an unfair method of competition and to summon persons and business organizations for hearings on the apparently unfair practice or method of competition. If after such an investigation and hearing the Commission determines that the practice or method of competition is unfair, it issues an order to the person or organization concerned to cease and desist from using these methods. This person or organization, the defendant, may petition for a review of the case and the "cease and desist order" may be modified or set aside. The defendant may ask for a review of his case by the United States Circuit Court of Appeals; if dissatisfied with the latter's decision, he can appeal his case to the Supreme Court of the United States.

To assist its members in conducting investigations, the Commission has the power to subpoena persons and to require the production of documentary evidence. Such evidence "includes

all documents, papers, correspondence, books of account, and financial" records.

On March 31, 1938 the Act was amended by the Wheeler-Lea Amendment. This amendment made it

> unlawful for any person, partnership or corporation to disseminate, or cause to be disseminated, any false advertisement—
>
> (1) By United States mails, or in commerce by any means, for the purpose of inducing, or which is likely to induce, directly or indirectly, the purchase of food, drugs, devices, or cosmetics; or
>
> (2) By any means, for the purpose of inducing, or which is likely to induce, directly or indirectly, the purchase in commerce of food, drugs, devices, or cosmetics.

The amendment explained that by the term "device" was meant

> instruments, apparatus, and contrivances, including their parts and accessories, intended (1) for use in the diagnosis, cure, medication, treatment, or prevention of disease in man or other animals; or (2) to affect the structure or any function of the body of man or other animals.

Before this amendment to the Act was passed, the Commission had been exercising power over false and misleading advertising of foods, drugs, and cosmetics. It had the authority to do this by the broad powers over unfair competition which were conferred on the Commission by the original Act.

In the course of its investigations the Federal Trade Commission has declared many practices and methods to be unfair competition. Some of these will be discussed below.

1. Misrepresentation. This kind of deception has taken many forms. One of the most common is false and misleading statements concerning the quality or composition of products. Most consumers are amateurs when it comes to judging the quality of the merchandise they buy, and they realize it. Numerous instances of misrepresentation and alleged misrepresentation of quality and composition have been brought before the Commission. Reputable manufacturers have realized that they have been injured by the false or misleading statements and claims made by those with a questionable reputation.

Consequently, there has been considerable agitation for labeling laws.

In 1939 this demand led to the passage of the Wool Products Labeling Act. The Act makes illegal the misbranding of wool products and requires whoever introduces a wool product into commerce to attach a label indicating the wool content of the product. The penalty for violating the Act is a maximum of one year imprisonment and a fine of $5,000. Agitation for more labeling laws of this kind continues.

The unwarranted use of foreign or domestic names, phrases, and other means suggesting that a product was manufactured in a locality reputed to produce articles of the highest quality has been frequently held to be unfair competition. The use of "Limoges" on chinaware and porcelain was ordered discontinued when the name was used to indicate that the article originated in France and such was not the actual case. Similarly the use of the words "English," "German," "Swiss," "French," "Belgian," "Irish," "Italian," and other place names has been ordered discontinued. In connection with rugs, the use of the words "Oriental," "Persian," "Chinese," "Kirman," and "Numdah" has been ordered discontinued when they were improperly used.

Misrepresentation of sales offers also has been condemned by the Commission. This practice has taken numerous forms which have been held to be unfair competition: the misrepresentation of cancellation privileges; the representation that a refund policy existed when such was not true; and the misrepresentation of terms and conditions as to coupons, deposits, and trial offers. One of the most overworked words in advertising is "Guarantee." The Commission has held it to be improperly used in a long list of cases.

Misrepresentation of trade status has often been determined a violation of the Federal Trade Commission Act. For example, sellers have claimed to be manufacturers, mills, packers, tanners, weavers, or other producers, but the facts were otherwise. Their appeal to prospective purchasers usually featured "save the middleman's profit by purchasing from the advertiser."

Various misrepresentations to dealers, salesmen, and agents

have also been held to be illegal. These misrepresentations have been in connection with consignment contracts, earnings, refunds, exclusive agencies, and sales assistance. Exaggerated statements to dealers on the demand for a product have been ruled unfair competition and ordered to be discontinued.

Misrepresentation of price, another very common form of deception, has been held to be illegal. The price has been represented as "special," "introductory," "below cost," "wholesale," "reduced," or "factory." The object was to lead prospective purchasers to believe that they could obtain a high-quality product at a reduced price.

2. Practices unfair to competitors. Misrepresentation to others is indirectly unfair to competitors who conduct their business on an ethical basis. The purchaser is deceived and the reputable firm loses business and perhaps suffers some of the stigma attached to the disreputable competitor. There are certain practices, however, which are more directly unfair to competitors. Among these are the disparagement and misrepresentation of a competitor or his product, the harassment of and interference with a competitor, and the simulation of a competitor's name, trademark, and advertising.

The Commission has issued cease and desist orders when false reports and statements have been issued concerning a competitor's financial standing, safety of products, performance of products, prices, and discontinuance of operations. Also held to be improper are (1) the acquisition of a competitor's trade secrets, (2) the inducing of breach of contract between a competitor and a customer, (3) the enticing of a competitor's employees to leave the employment of the competitor, and (4) the physical interference with a competitor's property. The Commission has also prohibited the using of containers, labels, trademarks, business names, signs, window decorations, store fronts, and product designs which are similar to those of a competitor.

3. Coercive and oppressive practices. Intimidating and coercing customers constitute unfair competition and the Trade Commission has ordered it stopped on numerous occasions. Among the methods which have been ordered stopped are

misrepresenting that accounts have been turned over to collection agencies or attorneys, misrepresenting the balance due on an account, threatening collection suits, threatening to compete, threatening to cease dealing, and shipment of unordered goods.

4. Combinations and monopolies in restraint of trade. Combinations of competitors to cut off trade or supplies from certain persons or groups have been declared illegal. Some retailers have made a concerted effort to prevent manufacturers or wholesalers from selling to certain types of competitors such as chain stores, mail-order houses, coöperatives and firms doing business both on a wholesale and retail basis. Manufacturers have acted to prevent other manufacturers from obtaining necessary raw materials and supplies. Such conspiracies in restraint of trade have been held to be illegal. It has not been held unlawful for a single firm to refuse to deal with another. If two or more firms, however, agree not to deal with another they are likely to be held guilty of unfair competition.

Combinations of competitors for the purpose of allocating customers, sales territories, pooling of business, or the curtailment of production have been held to be unfair competition. Producers have also been prohibited from using a common sales agency. Even coöperative action among competitors to bring about the adoption of a standard for their products has been questioned.

An exclusive dealing agreement between a buyer and seller has been held to be unfair competition. A manufacturer of automobile parts was prohibited from making or renewing contracts for the sale of such parts on the condition that the purchasers should not deal in goods obtained from the manufacturer's competitors. In the establishment of an exclusive agency, both parties to the agreement should exercise care not to in any manner restrain competition.

Tying agreements or contracts have frequently been ruled illegal. These agreements usually require the purchaser of one product to buy another item or he will not be permitted to secure the first product, which may be particularly desirable. The "block booking" of motion picture films, however, was

held to be fair competition. By this practice, an exhibitor of motion pictures must lease an entire block of films or none at all. Usually one or more films in the block are inferior attractions which exhibitors do not wish to show. To have the privilege of showing better attractions, however, they must also accept the inferior.

Price agreements of various kinds are illegal. Agreements between two or more members of an industry on the price at which they will sell their products have usually been declared to be unfair competition. Even resale price maintenance is illegal if the following conditions are not met: (a) the commodity which is the subject of the agreement bears, or its container bears, a trademark, label, brand, or other distinctive identifications; (b) the commodity is in free and open competition with other commodities of the same general class produced and distributed by others. Coöperation between competitors to maintain resale prices is illegal. Manufacturers cannot agree among themselves, wholesalers cannot agree among themselves, and retailers cannot agree among themselves to maintain resale prices.

5. Bribery. Commercial bribery, the practice of sellers paying money or making gifts to employees or agents (without the knowledge and consent of employers) to induce them to promote the purchase of the seller's goods, is unfair competition. Such secret dealings have been held to give the seller offering the bribe an unfair advantage over competitors.

Questions

1. When was the Sherman Act passed? What are its principal provisions?
2. Is intrastate commerce subject to the provisions of the Sherman Act?
3. What is interstate commerce?
4. What was the rule of reason?
5. When was the Robinson-Patman Amendment passed? What Act did it amend?
6. Does the Robinson-Patman Amendment prohibit all price discriminations?
7. What are resale price maintenance laws? How many states have such laws?

8. What was the Miller-Tydings Amendment? What Act did it amend?
9. What requirements must a product meet in order to be eligible for a resale price maintenance agreement?
10. Is it necessary to own a particular brand in order to establish its resale price?
11. Is it necessary to be a party to a resale price maintenance contract in order to be bound by the provisions of such a contract?
12. What are price-floor laws?
13. When was the Federal Trade Commission Act passed? What did it provide?
14. What did the Wheeler-Lea Amendment provide? The Wool Products Labeling Act?
15. What practices has the Federal Trade Commission declared to be unfair competition?
16. The old rule was that the buyer should beware. The new rule is that the buyer is not to be fooled nor deceived. How far should the courts go in protecting the buyers from their own ignorance and carelessness?
17. Is it true that honest business men are often forced to use dishonest practices because of unfair competitors?
18. The Haywire Company manufactures furniture out of chestnut and gum wood which it covers with a thin coating of mahogany veneer. It advertises its product as mahogany. Is this fair?
19. The Eveless Company manufactures furniture of soft wood and then stains the surface to resemble walnut. It marks its furniture American Walnut, Black Walnut, Red Walnut, and so forth. Is this unfair?
20. The Coonskin Company advertises coats made of muskrat skins as Canadian Seal, Siberian Seal, and Hudson Bay Seal. Is this fair?
21. A company located in New York State makes cigars from domestic tobacco which it sells as Havana cigars. It claims that Havana is a trade name used to denote its type of cigars. How about it?
22. The NoKnock Knitting Mills Company shows a picture of a large factory on its stationery and on much of its advertising matter. It does not own or operate any mills. It is purely a selling company. Is it guilty of unethical or unfair competition?

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Marketing Cost and Efficiency

THE QUESTION of marketing and distribution costs was brought into prominence about the opening of the twentieth century. The problem developed when production generally began to overtake demand; as the marketing problem became more acute, questions concerning the efficiency and cost of marketing were asked. As an aid in answering these questions the functional concept of marketing was developed. Today, however, it is still impossible to give a definite "yes" or "no" to the fundamental question: Does distribution cost too much?

What Is the Cost of Distribution?

Before any attempt can be made to answer the primary question, we must determine what constitutes the cost of distribution. Government bodies have investigated the distribution costs of particular kinds of commodities. The cost of marketing food products has usually been the subject of these investigations; masses of statistics have been gathered showing the costs of distributing oranges, bread, canned goods, meat, and other items. Normally, the starting point has been the price paid to the farmer for raw materials. This has been followed by an accumulation of data concerning the activities of the various middlemen and processors who handle the product after it leaves the producer until it reaches the consumer.

The difficulties and problems of making such studies have been enormous. Assumptions of one kind or another have

frequently been necessary. Usually sample data only have been obtained, and these, as a rule, for only one year. Many firms do not have adequate records. Numerous firms are engaged in the same industry but their operations are not strictly comparable. Some firms are unwilling to coöperate or refuse to furnish information. Nevertheless, a "cost of distribution" has been found for an industry or for a class of products.

A major difficulty in determining what is the cost of distribution is the fact that marketing conditions do not remain the same. Often the differences from one year to another are great. Marketing conditions in the years 1921, 1929, 1933, 1939 and 1947 certainly differed in many ways. Some years a seller's market exists, and in other years a buyer's market exists. The cost of marketing varies accordingly.

Another major difficulty is determining what elements of marketing will be investigated from a cost viewpoint. The logical procedure would be to tabulate a firm's costs of performing the marketing functions. Many investigators, however, appear not to know what the marketing functions are and they are unable to distinguish functions from the techniques of performing functions. Even when they are able to do so, they find that the firms which are willing to coöperate have not found it practical to separate the costs according to marketing functions. If an attempt is made to segregate the costs according to marketing functions, all the problems of expense allocation are confronted.

The costs of production must be segregated in order to arrive at the distribution cost of a product. Even the usual methods of determining the costs of production are arbitrary and sometimes more convenient than logical. The bases of allocating production costs are not generally agreed upon; they should vary from industry to industry and from firm to firm. It is convenient to consider the costs of some processing machines as production costs. Certain costs involved in making a stamping machine or a sealing machine may be considered production costs, but are all the costs of such machines properly considered production costs? It was necessary to buy and sell these

machines as well as the materials from which they were manufactured.

In the face of all these difficulties, investigators have arrived at a cost of distribution. The less informed and those seeking to use the information for biased purposes have forgotten or ignored the assumptions and conditions under which the investigation was made. Misinformation and half-truths have been passed on as fact.

Too Much by What Standard?

To answer the question, Does distribution cost too much? some standard of comparison must be used. A possible standard may be the costs of distributing the product in some previous period.

Over a period of time the methods of marketing a product are changed. At one time almost all meat was sold directly by the producer in public markets. Very little is sold this way in the United States at present. A comparison of the marketing cost of meat in 1800 with the cost of marketing at the present would mean little. Much of the work of production and marketing was performed by the farmer himself. His money outlay for marketing was small and to allocate costs for that time would be an unsatisfactory method of determining costs. Even should the relative cost of marketing be found to be lower in 1800 than at the present it could not be inferred that the marketing methods of 1800 are to be preferred over those of the present.

The cost of marketing a product includes the cost of extending credit and making delivery and other services which the consumer prefers that middlemen and manufacturers perform. In some periods, the consumer performs these services for himself or foregoes the services. During World War II the consumer performed more of the delivery service than formerly. He asked for less credit because he needed less credit. There were fewer salesmen. The cost of marketing may have declined but so did the amount of marketing service which was performed. The consumer was not obtaining the same produc

and service which he had obtained previous to the War. To compare the costs of marketing, the same things must be compared. A product marketed with certain services is not the same as a product marketed without those services.

In attempting to determine whether distribution costs too much, the cost of marketing one product might be compared with the cost of marketing another. If the method of marketing the two products is different, the comparison is not sound. Furthermore, the products may be designed for different uses or markets, and if so, their marketing costs will undoubtedly be different.

It might be possible to segregate the marketing cost from the production cost and then compare the two. The cost of marketing the product may be greater or less than the cost of producing it, but can it be said that the marketing cost is too high? If the cost of marketing is higher than the cost of production, perhaps it should be still higher in order to increase sales. Lower production costs may follow from the increased volume of goods sold due to the increased marketing effort. If the marketing cost is lower than the production cost, perhaps it should be still lower. It is not to be assumed, because the cost of marketing is any amount, that it is as low as it should be.

There are times when costs or prices are too high. These times are when many consumers cease buying. Prices then begin to decline because they are too high in comparison with what the consumer can pay or desires to pay. It probably can not be said definitely whether it is the costs of production or the costs of distribution which are too high. Perhaps it is both. Total costs or prices may decline considerably. Either production or marketing costs may increase relatively at such a time. For example, if the consumer price of an article is $1.00, and it is assumed that marketing costs are 50 cents and production costs are 50 cents, the cost price of the article may decline to 60 cents before it can be sold in the same quantity as when its price was $1.00. If marketing costs are now assumed to be 40 cents and production costs 20 cents, the cost of marketing has increased relatively from 50 per cent to 66⅔ per cent. Apparently this cost of distribution is not too much since the article

is selling in the same quantity in which it previously sold. Whether it is marketing costs or production costs, or both, which have been too high preceding a period of declining prices may, therefore, be unknown. All that is known is that the combined costs have been too high.

Reducing the Cost of Distribution

Though it may be difficult to determine the cost of distribution, it is most desirable to develop a more economical system of distribution. Several proposals have been made for improving the efficiency of our distributive organization. Some of these will be discussed.

Elimination of wasteful competition. Some competition is, or is assumed to be, wasteful. There is no apparent justification for it. It is not easy to establish a standard by which all competitive effort can be judged to be wasteful or not wasteful. It is impossible to establish any set of standards which are accepted by all. Even if a set of ideal and specific standards were established, the universal application of them would be an intensely difficult problem.

It is possible to say that inefficient competition is wasteful—that the manufacturer, wholesaler, or retailer who operates at a loss is inefficient. He does not understand his job well enough to be able to serve society efficiently. His effort would be better expended at something where he could be productive. But from a broad social view, can it be said that the competition of the loser is undesirable? Would those who are able to earn a profit by serving society efficiently make as much effort to be efficient if they were not faced by those who are less efficient? It is doubtful that their efforts would be as concentrated.

It is entirely possible to devise a set of standards which would reduce greatly the number of business organizations that serve society at no gain to themselves. Those who could not meet the standards established for a given line of business would not be permitted to enter that business. This policy is not advocated here. It is contrary to that fundamental freedom—the freedom of opportunity. The price of wasteful competition is an infi-

nitely small price to pay for this freedom. Improving the competitive efficiency with which society is served should be approached from a different point of view.

At least one viewpoint from which the approach should be made is that of education, training, and the supplying of information. An informed, trained competitor will not commit the characteristic errors of the uninformed. Too many people enter various lines of business activity with a minimum knowledge of the business and inadequate training for it. Formal business training is highly desirable and, in the long run, less expensive. It provides basic knowledge in less time and more economically and efficiently than does informal training which may be self-administered and unorganized. Neither formal nor informal training can absolutely guarantee results. There is no certainty that the trainee will be able to apply his knowledge with a high degree of efficiency, but the surveys which have been made of those who have had a formal business training indicate that the probabilities of successful application are very high.

The information concerning a line of business endeavor must originate with those who are presently successfully engaged in the industry. It may be supplied by individual business organizations but it can be supplied more economically by a trade association or some branch of the government. Much information has been made available but too frequently it has failed to inform adequately, or the novice by himself has been unable to gain much from the data.

Fraudulent and deceptive competitive efforts are wasteful. They harm both other competitors and consumers. The consumer is harmed because he receives nothing or something less than was expected for the price he paid. The legitimate competitor is harmed because he was prevented from serving the customer. At times it is difficult to determine whether or not fraud or deception was involved but this is not true in the majority of instances. The courts have long had the authority to stop anti-social business practices but the criticism has been made that not enough of these cases have been brought into the courts and the penalties when inflicted have been too light.

There is merit in these criticisms. Better training of business men will reduce the amount of fraud and deception. A well-trained business man knows that he will be successful by using legitimate methods and that eventually any gain made by using illegitimate methods will be lost.

Better Business Bureaus have achieved some success in discouraging fraudulent and deceptive practices. These organizations supported by local business men have developed because the members are aware of the damage which those who practice fraud and deception can do to the reputation of men who follow sound ethical practices.

Reducing the number of middlemen. It has been pointed out frequently that there are too many middlemen. But what is meant by "too many middlemen"? It may mean that there are too many merchants in a single line of business or it may mean that a certain commodity is handled by too many middlemen before it reaches the ultimate consumer. The very small sales volume of some retailers is taken as indication that there are too many of them. It is expensive for wholesalers and manufacturers to service small retailers. The cost of handling the orders for these retailers is high. They order frequently and in small amounts. It is as expensive to service one of these small accounts as it is one several times as large. Yet should these small retail businesses be eliminated and prevented? Some of the largest retailers today were small retailers yesterday. By careful management they grew into large and successful stores. Not all retailers can begin on a large scale. Many small retailers are located in small towns and thinly populated territories. For the people in these locations the small retailer performs a very valuable service.

Before they reach the ultimate consumer some products are handled by several middlemen. Cotton and grain, for example, are handled by several different business organizations. Frequent investigations of the number of middlemen handling various products have been made, but no unqualified, general conclusion that too many middlemen were handling the product has been established. Instead, these government investigations have often indicated the importance of the various services

performed by the different kinds of middlemen. It has also been discovered that some products were handled without advancing the product in the direction of the consumer. Wholesale merchants, for instance, have been found to be making sales to each other. The amount of such selling, however, is small and it may result in consumers being served somewhat more quickly than they would otherwise. Sometimes a wholesale merchant's stocks may not include the item ordered by the retailer. To provide quick service to the retailer, the wholesaler obtains it from another wholesale merchant who carries the merchandise. A sale in the same stage of distribution occurs without advancing the product in the direction of the consumer.

There are other conditions which give rise to a purchase and sale in the same stage of distribution. Strictly speculative exchanges, for example between cotton and grain merchants, have been questioned from a broad social viewpoint. Perhaps some of this speculation can not be justified, but probably cotton and grain would not be distributed as efficiently as it is if all speculation in these products was prohibited. Successive government investigations have brought out persisting inefficiencies in the distribution of these commodities.

The use of coöperative methods. Many persons believe that the substitution of coöperative methods of marketing for private organizations will reduce the cost of distribution. In the marketing of agricultural products coöperative organizations have made some progress. Farmers aware of prices in the central markets believed that the prices paid to them by local private buying organizations were too low. If products were consigned to a commission merchant in a central market, the farmer had no assurance that the commission merchant had put forth his best effort for his principal. Prices at which a farmer's product was sold were often below what the top of the market had been for the day. A local organization composed of and operated by farmers had more appeal. It could eliminate the middleman's excessive profits. Many coöperative organizations have been fostered and supported by the Federal Government.

Have coöperative agricultural organizations reduced the cost

of marketing farm products? An unqualified affirmative answer can not be given to this question. When a local coöperative organization replaced a private buying and handling organization, it had to take on the functions formerly performed by the private organization. If members of the coöperative performed some of the work of the organization without pay, the money cost of the coöperative organization would probably be less than the expenses of the organization which it replaced. If the cost of the contributed services were added to those for which no money outlay was made, the total cost of the organization over a period of time might not be less, however, than for the private organization.

Although there may be uncertainty as to whether or not the marketing cost was reduced by the local coöperative organization, there is one thing about which the members of the coöperative were certain: the elimination of many of the petty frauds perpetrated by some local dealers in the grading and weighing of farm products. When central market facilities were established by the coöperatives, there was a feeling that the products were handled fairly in the central markets.

Retailers have also attempted to reduce the cost of distribution by forming coöperative organizations. Efforts have occurred chiefly in the food trade. An examination of the expenses of the coöperative chains formed by retail grocers indicates that a small saving is made by these organizations as compared with the expenses of some service-type wholesale merchants. Such chains do not seem to have an advantage over the cash-and-carry wholesale merchants. However, if consideration were given to the free services performed by the members for the organization and to the services foregone but provided by the service-type wholesale merchant, it might be that the coöperative chain or retailer-operated wholesale house would be seen to have less of an advantage than it appears to have.

Retailers have also coöperated in buying, advertising, providing delivery service, and in collecting and dispensing credit information. Some reductions may be made in the buying expenses of retailers and the selling expenses of manufacturers and wholesalers when retailers form buying groups and pur-

chase in substantial lots. It is well known that hand-to-mouth buying as practiced by retailers is expensive both from the seller's and buyer's point of view. Coöperative newspaper advertising by independent grocers appears to be more effective than when each advertises independently. Newspapers also may grant some reduction in space rates because of the larger amount of space used by a coöperative advertisement. Coöperative retail delivery service reduces the amount of equipment needed to provide service. It eliminates duplication of service and it may discourage the consumer from requesting unreasonable service. Retailers have also been able to make economies in the collecting and dispensing of credit information by using coöperatively operated credit bureaus. They can reduce the expense of extending credit and at the same time be more effective. More credit information can be gathered at less expense when a central organization does it for all retailers in a community. The economies of coöperative advertising, buying, delivery, and handling of credit information may be small when compared with any total cost of the performance of these services but it is the many small economies which make the large saving.

Consumer coöperation in distributing merchandise as exemplified by the consumer's coöperative retail store has been promising but in general ineffective. Small savings have been made by operating these stores but the amounts have been so small that they are regarded as insignificant by most Americans. Furthermore, the immediate future for this method of reducing the costs of marketing does not seem to be particularly promising. The chain store and the efficient independents seem to do the work of retailing more effectively. Many coöperatives distributing farm supplies and equipment have been quite successful. Though farm supplies and equipment are, in a broad sense, industrial goods rather than consumer goods, the economy in the distribution of these goods has been of some significance and seems to have greater possibilities.

Consumers have made an important saving in the financing of their purchases by organizing credit unions. The cost of extending credit to consumers has been substantially reduced

by these unions as compared to the cost when dealing with small loan companies and firms selling merchandise on an installment basis. The small loan companies and installment firms charge rates of interest as high as 42 per cent per year whereas the credit unions frequently have charged only 6 per cent.

Aid for the consumer. Owing to the wide range of commodities and services from which the typical consumer may choose, it is believed by some that he is generally an incapable buyer and needs more product information. That consumers have but little real knowledge of most of the merchandise they buy can be demonstrated easily by anyone who has a professional knowledge of a given product. But the question arises—Is it necessary for every consumer to have a professional knowledge of all the merchandise he buys? A great deal of merchandise is consumed satisfactorily without a technical or professional knowledge of it. Though it may be desirable for the consumer to have such knowledge, will he take the time to inform himself even if the information is supplied? He can not be forced to obtain such knowledge against his will.

Certain practical difficulties are involved in giving the consumer "product knowledge." There is often more than one basic system of operation for mechanical products. Sometimes engineers themselves are in disagreement as to which is the best system. How can the untrained consumer be expected to determine which is best when the mere problem of understanding the facts is an overwhelming obstacle for some people? There is also the problem of making use of the knowledge at the time of purchase. Special tests are needed to determine definitely the quality of some merchandise. Retailers would not, for example, permit the opening of canned foods by every consumer for the purpose of determining the quality.

How shall product information be made available? Shall the Federal Government undertake to find out all a consumer should know about the merchandise he buys and send the information to all consumers? Some progress in providing product information has been made in home economics classes. It may be that the public schools are the best channel of providing product knowledge. Legislation which requires that certain

product information be placed on labels attached to the product has also aided the consumer education program. The very fact that the manufacturer must place the information on the label and that retailers are aware of the information on the label may eliminate some deception and misunderstanding.

From time to time it has been pointed out that the retail or wholesale costs of the raw materials from which a product is made are but a fraction of the final retail price charged the consumer. The material in a product selling at $30 may be equal in quality to that selling at $60, but these explanations are often one-sided. It should also be pointed out that there is a difference in the quality of workmanship used in manufacturing the two articles. Above all, a colossal lack of knowledge is evident regarding the many steps required to bring a product from its raw material stage to the point of being used by the consumer. It is a very common error to assume that nothing of value is added to a product beyond the cost of manufacturing. This phase of consumer education warrants much more attention. Very few people have had a high school course in economics, to say nothing of a course in marketing. They have not grasped the full meaning of time and place utility and the magnitude of the problems involved in creating these utilities. Yet they establish themselves as critics of our marketing organization.

Fashion is another factor frequently overlooked by those whose critical approach to marketing is by the method of pointing out the difference between the cost of the raw material and the price paid by the ultimate consumer. Whether he should or should not, the consumer places a value on being in fashion. He is willing to pay a higher price for an article that appeals to his esthetic sense. He will reject quickly something that is not of the proper color and line. It makes no difference that the products are composed of identical raw materials or semifinished goods. Furthermore, dame fashion is fickle. No sooner is a particular style "in fashion" than attention is directed to another, only to have it soon run its race and be superseded by others. Catering to the whim of fashion is expensive when measured in the man-hours, machine-hours, and materials

which are lost because consumers no longer prefer the lines or color of some product. Merchandise must be sold at a loss by manufacturers, wholesalers, and retailers unless they anticipate and provide for these shifts in taste. Expenditures for merchandise which has become unsalable will not be recovered unless advance provision is made for the possibility that the consumer will suddenly change his mind concerning the prevailing fashion. Usually the merchant charges a price high enough for such merchandise to cover the loss on any left-overs.

Standardizing and simplification. To aid in reducing the cost of distribution it has been advocated from time to time that additional commodity standards be established and accepted. In situations where the policy could be applied, it would, in the long run, somewhat reduce the cost of distribution. But it probably has a limited application in the field of style goods. The consumer, if permitted the expression of a free choice, will accept little curbing of his desire for distinctiveness in style. Under the stress of special circumstances, such as war, government decree may curb this desire for a short period, but in a democratic country this type of interference with individual freedom will not be tolerated indefinitely. Manufacturers can do much to bring about the acceptance of standards and the simplifying of products. Consider, for example, the widespread adoption of basic colors for the home furnishings industries. Yet manufacturers must not too drastically reduce the available number of colors or the consumers will encourage manufacturers who will cater to their desires.

It is generally recognized that catering to consumer desires has led to much diversification of products. From time to time manufacturers individually and through their trade associations have also promoted simplification by reducing the product varieties of their industries. By producing a simplified line, some of the risk of loss due to style obsolescence can be avoided with a probable saving to the consumer and the seller. A smaller number of articles of unwanted design and color will need to be carried by the price of those which are wanted.

There has been much agitation for the establishment of standards for canned foods and consumer education on the ne-

cessity of such standards. This has arisen because of the multiplicity of brands, can sizes, quality, and advertising claims. Nowadays, to obtain the most for his money, the consumer must exercise some fine discrimination; we are only assuming, however, that the consumer has the time and knowledge to do so. The establishment of standards for canned foods merits all the attention it has received, but so far little progress has been made. Numerous manufacturers and distributors of these products have been opposed to the establishment of standards for consumers. They have spent large amounts in getting their brands established and accepted by consumers, and the establishment of general standards and the education of the consumer concerning these standards might destroy this goodwill. In some instances the consumer would discover that the brand of an unknown manufacturer or distributor was equal in quality and perhaps lower in price than the highly advertised products. The opponents of such standards emphasize that there are some very practical difficulties involved in establishing these standards: that processes of packing and preparing differ, crop qualities differ from year to year depending on weather conditions, and that any set of standards consequently would be complex and confusing.

Conclusion. Many people engaged in marketing will readily admit that the efficiency of marketing can be improved just as many persons engaged in manufacturing will agree that the efficiency of manufacturing can be improved. The methods of improving marketing efficiency to reduce the cost are many. The relative effectiveness of these various methods in reducing the cost of marketing is a matter of some disagreement. The most effective methods seem to be wisely regulated competition and better-trained business men. Intelligent use of the other methods which have been discussed may result in significant improvements.

Questions

1. Name some of the difficulties encountered in determining what is the cost of distribution.

2. Can one construct a generally accepted standard for determining whether or not the cost of distribution is too high? If so, indicate what such a standard should be.
3. What is wasteful competition? How can it be eliminated?
4. Are there too many middlemen? If so, how should the number of them be reduced?
5. Have coöperative agricultural organizations reduced the cost of marketing farm products?
6. What coöperative methods have retailers used in attempting to reduce the cost of marketing? How successful has each of the methods been?
7. Has consumer coöperation reduced the cost of marketing?
8. Will the distribution of product information among consumers tend to reduce the cost of marketing? If so, how shall this information be collected and distributed?
9. Will the establishment of commodity standards reduce the cost of marketing?
10. What are some proposals, other than those mentioned in this chapter, for reducing the cost of marketing?
11. What are probably the most effective methods of reducing the cost of distribution?
12. Does the fact that the department store performs the wholesale function reduce the total marketing cost?
13. The offering of so many services by sellers is given as one reason for the high cost of distribution. Some people assume that these services are rendered by the sellers in the competitive struggle for business and that the consumers are injured by the high cost of rendering these services. Do you agree? Why or why not?
14. Why does the price received by the farmer constitute such a small part of the price paid by the consumers for finished goods made from farm products?
15. What is meant by cost accounting? What has it done for manufacturing during the past years? Do you believe that it can make any equally valuable contribution to marketing?
16. Large-scale production is said to reduce production costs. Large-scale production means the concentration of production in a few large plants. These plants are located at a distance from many consumers. These large companies are said to have high distributing costs as a result of the "high-pressure" selling necessary to sell enough goods to keep their plants operating at capacity. Goods must be transported for long distances. Distribution costs are said to be increased. Do you agree? Granting for the moment that distribution costs are increased, are the consumers injured by the increased costs? Why or why not?

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